FEDERAL FARM LOAN ACT CASE.

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1919.

No. ~~592~~ 199

CHAS. E. SMITH,

Appellant,

vs.

KANSAS CITY TITLE & TRUST CO., ET AL.,

Appellees.

Appeal from the District Court of the United States for the Western Division of the Western District of Missouri.

BRIEF FOR APPELLANT

In support of the contention that the Farm Loan Act is unconstitutional in so far as it (1) authorizes the creation of Joint Stock Land Banks and (2) exempts from State taxation farm mortgages and Farm Loan Bonds, whether issued by Joint Stock Land Banks or by Federal Land Banks.

FRANK HAGERMAN,
WM. MARSHALL BULLITT,
Counsel for Appellant.

INDEX

LIST OF AUTHORITIES.

Historical Authorities.

FEDERAL FARM LOAN ACT CASE.

IN THE

Supreme Court of the United States.

OCTOBER TERM 1919.

No. 593.

CHAS. E. SMITH, *Appellant,*

vs.

KANSAS CITY TITLE & TRUST CO., ET AL., *Appellees.*

Appeal from the District Court of the United States for the Western Division of the Western District of Missouri.

BRIEF FOR APPELLANT.

This appeal challenges the constitutionality of the FEDERAL FARM LOAN ACT of July 17, 1916 (39 Stat. 360) upon the ground that Congress had no power (1) to establish the system of Federal Land Banks, and especially of Joint Stock Land Banks, therein created; nor, in any event, (2) to exempt the farm mortgages and bonds, issued thereunder, from State taxation,—the latter ground being the

one upon which Senators SUTHERLAND, MCCUMBER, CUMMINS and others opposed the passage of the Act in the Senate, in elaborate arguments which well repay perusal (see 53 Cong. Rec., pp. 6961-6965, 6968, 7245-7246, 7305-7317); and about the constitutionality of which its author (Senator HOLLIS), and its principal advocates had such grave doubts, that they openly admitted the necessity of adding some incidental features to the Act in order to give it a semblance of validity. (53 Cong. Rec., 6861, 7026, 7129, 7246, 7310. See also 6793, 6795-6.)

Its constitutionality would have been questioned earlier but for the Government's vigorous opposition to any attack on the Act during the war. The nullification of the Act would not cause the bonds heretofore issued to be a loss to the holders thereof (as the farm mortgages are a valid security), but it would merely subject them to State and Federal taxation. THE TAX EXEMPTION QUESTION IS THE REAL ISSUE SOUGHT TO BE SETTLED HERE.

STATEMENT OF THE CASE.

THE KANSAS TITLE & TRUST CO. was about to invest a large amount of its corporate and fiduciary funds in the purchase of Farm Loan Bonds issued respectively by Joint Stock Land Banks and by Federal Land Banks, solely because the company believed the bonds to be wholly tax exempt. (R. 11-16.)

CHAS. E. SMITH, a director and large stockholder in the company, objected to the proposed investment upon the ground that the tax exemption was void and the bonds were taxable; he voted against the resolution of purchase and then filed this suit in the District Court to enjoin the company from purchasing the bonds. (R. 15, 1.)

A Federal Land Bank and a Joint Stock Land Bank intervened and were made parties defendant; the ATTORNEY GENERAL of the United States appeared as *amicus curiae;* a motion was made to dismiss for want of equity; the motion was sustained; the plaintiff declined to plead further, the bill was dismissed, and this appeal was taken. (R. 19, 21, 30.)

THE FARM LOAN ACT.*

The sole purpose of creating the Farm Loan System (as the Act's language proves and as avowed in the Debates, in the various Committees' Reports, in the Government's official announcements, and in the literature cited in the margin*) was to enable owners of farm lands (not necessarily farmers) to borrow money on farm mortgages for *very long* terms (up to forty years), at extremely *low* interest rates.

Disregarding the numerous, badly arranged, confusing, needlessly complex and cross referenced *administrative* provisions, the Act provides for a system by which (*a*) farm lands

*The history of the movement to establish in the United States a system of rural credits based on the German plan of collective and co-operative borrowing and lending of money on long time farm mortgages can be found in "Agricultural Co-operation and Rural Credit in Europe" (1913) 63d Cong. 1st Session, Senate Doc. Nos. 17 and 214, Parts I, II and III; Id., 2d Session, Report of the American Commission (1914) Senate Doc. No. 261, Parts I, II; Id., Report of the U. S. Commission on Agricultural Credit (1914) Senate Doc. No. 380; 64th Cong. 1st Session, "Report of Joint Committee on Rural Credits" (1916) House Doc. No. 494; Id., "Report of Committee on Banking and Currency" (1916) House Report No. 630; Id., Conference Report (1916) Senate Doc. 472; See also "Rural Credits" (1915) 64th Cong., 1st Session, Senate Doc. No. 9; 63d Cong. 1st Session (1913) Senate Doc. No. 114; Hearings before the Subcommittee of the Committee on Banking and Currency (H. R.) on "Rural Credits" (1913); and Joint Hearings before the Subcommittees of the Senate and House Committees on Banking and Currency on "Rural Credits" (1914).

can be mortgaged to private investors, and (*b*) the mortgages, and the bonds secured thereby, will be wholly exempted from all State, Federal and municipal taxation, whether *ad valorem*, income or inheritance.

A twofold result is achieved; *first*, by virtue of the tax exemption, these particular farm mortgages bear a slightly lower interest rate than they would bear if they were taxable as Government bonds and other securities are taxed; *second*, a valuable form of private investment* is provided which enables persons of large wealth to avoid all income and supertaxes, so that a Farm Loan Bond in the hands of a wealthy man returns the equivalent of about 18 per cent per annum. (See advertisement of Joint Stock Land Banks as frontispiece.)

Merely to accomplish those two results, has the Federal Government express or implied power, under the Constitution, to forbid the States from taxing such mortgage bonds held by their citizens,—a species of property always recognized as subject to State taxation?

*See *Farmers Bank* v. *Minnesota*, 232 U. S. 516, 527-528; Cf market price of Liberty Bonds (91 to 99) with that (102) of Farm Loan Bonds!

The Act creates two distinct agencies for carrying out its objects, *i. e.*, Joint Stock Land Banks and Federal Land Banks, which must be considered separately.

I. JOINT STOCK LAND BANKS.

Any ten private individuals (bankers, merchants, or anyone at all) can organize a Joint Stock Bank with not less than $250,000 capital stock, which is authorized to lend money to *any person*, for *any purpose*, in *unlimited* amounts, repayable by small annual amortization payments in from five to forty years, on first mortgages of farm lands, regardless of whether the land is improved, occupied or even cultivated; and the bank can then issue its own collateral trust bonds, called "Farm Loan Bonds,"* which are to be secured by a deposit with a trustee, of the original farm mortgages and notes. (§ 16.)

The Act expressly provides that the Joint Stock Banks shall have *no power* (§ 16)

> "*to receive deposits* or to transact any *banking* or other business not expressly authorized by the provisions of this Act."

*The Farm Loan Bonds issued by the Joint Stock Banks are to be of such form and color as to be readily distinguishable from those of the *same name* but issued by the Federal Land Banks. (§ 16.)

The only business "expressly authorized" by the Act (except to lend on farm mortgages and to issue its bonds secured thereby) is (1) that they may buy and sell Government bonds (§ 13, Clause Eight) which anyone may do; and (2) a potential possibility of acting as depositary or financial agent for the government under § 6, which was inserted in an effort to make the Act constitutional.

> "SEC. 6. That all Federal Land Banks and Joint Stock Land Banks organized under this Act, *when designated* for that purpose by the Secretary of the Treasury, shall be depositaries of public money, except receipts from customs, under such regulations as may be prescribed by said Secretary; and they may also be employed as financial agents of the Government; and they shall perform all such reasonable duties, as depositaries of public money and financial agents of the Government, as may be required of them.
>
> And the Secretary of the Treasury shall require of the Federal Land Banks and Joint Stock Land Banks thus designated satisfactory security by the deposit of United States bonds or otherwise, for the safekeeping and prompt payment of the public money deposited with them, and for the faithful performance of their duties as financial agents of the Government.
>
> *No Government funds deposited under the provisions of this section shall be invested in mortgage loans or farm loan bonds.*"

27 Joint Stock Banks have been organized by private persons exclusively, with $8,000,000 capital stock; and they have issued $41,000,000 of their obligations, *i. e.*, Farm Loan Bonds secured by ordinary farm mortgage notes. (R. 5, 9.)

None of those banks have ever been designated as depositaries of public money nor have they ever performed any duties as financial agents of the Government. (R. 10.)

The Federal Government can never have any financial interest in these banks; nor can the banks receive deposits,* discount paper,

*While a Federal Land Bank is prohibited from accepting deposits from anyone "except from its own stockholders" (§§ 13, 14), the prohibition against a *Joint Stock Bank* accepting deposits is *absolute and unqualified.* (§ 16.) Hence Joint Stock Banks cannot even accept deposits from their own stockholders.

It may be suggested that § 16 provides that Joint Stock Banks shall have the powers of, and be subject to the restrictions and conditions imposed on, Federal Land Banks "except as otherwise provided," and "so far as such restrictions and conditions are applicable"; and, therefore, that the Joint Stock Banks are entitled to receive deposits from their own stockholders. However, it is quite obvious that they have no such power and it cannot be conferred upon them by any such an involved construction by reference. A subsequent portion of the same section provides expressly that they shall have *no power to receive deposits;* and this prohibition is *absolute* as to Joint Stock Banks, while it is expressly *qualified* as to Federal Land Banks by permitting the latter to receive deposits from their stockholders. Therefore, Joint Stock Banks cannot have the same powers as Federal Land Banks with respect to deposits.

lend money, deal in gold, silver, stocks, bonds (except U. S. bonds), foreign or domestic exchange, or do any of the other things which constitute the banking business.

The 27 Joint Stock Banks are "wholly owned" by "numerous private persons" (R. 5, 9),

> "who are operating and will operate such Joint Stock Land Banks *purely and exclusively for their own individual and private profit* as in the case of any other purely private corporation."

Nevertheless, the mortgages taken, and the Farm Loan Bonds issued, by this exclusively private money lending company, are wholly exempted from every form of taxation, § 26 providing:

> "First mortgages executed • • • to Joint Stock Land Banks, and Farm Loan Bonds issued under the provisions of this Act, shall be deemed and held to be *instrumentalities of the Government* of the United States, and *as such they and the income derived therefrom, shall be exempt from Federal, State, municipal and local taxation.*"

It is difficult to see exactly how (*a*) farm mortgages executed to a purely *privately* owned corporation and (*b*) the latter's obligations when held by *private* investors, can be

deemed "*instrumentalities* of the Government of the United States," and *hence,* with the income therefrom, *exempt from State taxation.*

Can the constitutionality of an Act authorizing private individuals to engage in the private business of lending on farm mortgages for private profit, be sustained (and their obligations when sold and owned by *private investors,* be exempted from all State taxation) by the simple expedient of *calling* them "instrumentalities of the Government" and of *authorizing* the Secretary of the Treasury to use them as Government depositaries or financial agents, although he has never in fact so used them? If so, what limit remains on the powers of Congress?

The Act also authorizes the creation of 12 additional banks, called Federal Land Banks, whose powers should be much more restricted than the Joint Stock Banks with respect to the *location* of the farm lands, the persons who might become *borrowers,* the *amount* of the individual farm mortgages permitted, and the *purposes* for which the loans must be made. They will now be considered:

II. FEDERAL LAND BANKS.

The Act provides that—

1. Twelve Federal Land Banks shall be organized, each with a minimum capital stock of $750,000, divided into $5 shares.*

Each of these banks is prohibited from accepting any deposits (except from its own stockholders, who, being borrowers, are not likely to be depositors to any considerable extent), or from paying interest on deposits, or transacting any banking business or indeed any other business not expressly authorized by the Act.

2. These banks are authorized to do but three things:

First. To lend (under a complicated plan of co-operative and collective groups of actual farmers called Farm Loan Associations), not exceeding $10,000 to any one person upon a long term, first mortgage on farm lands (where the proceeds of the loan must be used

*Any part not subscribed for in 30 days by the general public, was to be temporarily taken by the United States, which should receive no dividends or other return thereon during the time of its temporary investment. Provision is made for the gradual retirement of the stock thus subscribed for by the United States, so that in a few years the stock will all be owned by the borrowers, thus imparting a certain co-operative or mutual feature to the management.

exclusively for the purchase or improvement of, or the refunding of a prior mortgage upon, farm lands), repayable in from five to forty years by small annual amortization payments.

Second. To issue and sell to the investing public, their own collateral trust bonds called Farm Loan Bonds, secured by the deposit with a trustee of the individual farm mortgages so taken.

As the insignificant capital of the banks would be quickly exhausted by the first loans (and as deposits could not be accepted), the only way the banks could obtain funds with which to make further loans, would be by selling the mortgages they had already taken. Instead of selling the individual mortgages of particular farmers, the collateral trust bond was adopted as more likely to prove attractive to the investing public.*

Third. To buy and sell United States bonds.

3. These banks (like the Joint Stock Banks) may be designated by the Secretary of the Treasury as depositaries of public money, and as financial agents of the Government; and (unlike the Joint Stock Banks), the Secretary of the Treasury is authorized to "make depos-

*The collateral trust bonds are also made the joint and several obligation of the twelve Federal Land Banks, thus making them a safer security than the individual farmer's mortgage would be, even if endorsed by a single Land Bank.

its for the temporary use of any Federal Land Bank" upon which it shall pay interest to the Government, such deposits to be callable at the demand of the Secretary and never to exceed $6,000,000 in the aggregate. (§ 32.)

4. Complete tax exemption is given in the following language (§ 26):

> "That every Federal Land Bank and every national farm loan association, including the capital and reserve or surplus therein and the income derived therefrom, shall be exempt from Federal, State, municipal and local taxation" [excepting taxes upon its office and real estate taken for debt].
>
> "*First mortgages* executed to Federal Land Banks * * * and *Farm Loan Bonds* issued under the provisions of this Act, *shall be deemed* and held to be *instrumentalities of the Government of the United States,* and as such they and the income derived therefrom, shall be *exempt* from Federal, State, municipal and local taxation."

12 Federal Land Banks were duly organized; the public took but a small amount of stock, and the United States temporarily subscribed for nearly $9,000,000 stock, which has since been reduced to $8,265,809. (R. 3, 9.)

These Federal Land Banks have loaned large sums on farm mortgages, repayable in

annual amortization installments extending over 36 years; have deposited the mortgages and notes with a Trustee (Farm Loan Registrar) and have issued against them $285,600,000 of their own collateral trust obligations, called Farm Loan Bonds, due in 20 years, of which $135,000,000 were purchased and are held in the Treasury of the United States, under an amendment of July 18, 1918. (40 Stat. 431; R. 4, 9.)

None of the banks have ever been designated as depositaries of public money,* nor employed as financial agents of the Government excepting that three of the Banks assisted in making some seed grain loans to farmers out of the President's $100,000,000 war fund. (R. 10.)

These banks, like the Joint Stock Banks, are prohibited from doing practically anything that is ordinarily embraced under the term banking business. They cannot receive deposits (excepting from their own stockhold-

*Under § 32 of the Act, the Secretary of the Treasury, shortly after the Banks were organized, made some deposits in the nature of loans for their temporary use, upon which they paid interest as upon a loan, all of which deposits or loans have been repaid to the Government. (R. 10: 2d Annual Report of Farm Loan Board, p. 9.)

ers), discount paper, deal in gold, silver, foreign or domestic exchange, bonds (except United States Bonds), or indeed do anything in the nature of a banking business. They are strictly confined to making loans on farm mortgages, to the issuance of Farm Loan Bonds (secured by deposits of such mortgages), and to the investment of the resulting funds in other farm mortgages or Government bonds.

What Federal function is performed by these banks to authorize the exemption of the mortgages and the Farm Loan Bonds in the hands of *private individuals,* from State taxation?

Amendment of January 18, 1918. There was such grave doubt as to the constitutionality of the Act, that notwithstanding complete tax exemption, the investing public would not purchase the Farm Loan Bonds; and consequently the banks, having quickly exhausted their limited capital, were unable to continue operations. An appeal was made to Congress; and, in the midst of the war, when the Government was straining every effort to sell its own bonds to meet war expenses, an Act was passed authorizing the Secretary of the Treasury to

buy $200,000,000 of Farm Loan Bonds. (40 Stat. 431; Farm Loan Board's 1st Annual Report, p. 18; 2d Annual Report, pp. 15-16.)

In other words, the money raised by the Government for war purposes through taxation and the sale of Liberty Bonds, has been to the extent of about $150,000,000, devoted to the purchase of Farm Loan Bonds in order to furnish the funds to lend to farmers at low rates of interest, and to afford an investment for wealthy persons which should be tax free. (R. 9.)

No constitutional objection is made to this use of Government money, as it can be sustained under the power of appropriation. The attack is made on the Act as it relates to the bonds sold to private investors.

ASSIGNMENTS OF ERROR.

The Court erred in sustaining the constitutionality of the Farm Loan Act, especially as applied to the Joint Stock Land Banks, and to the tax exemption of Farm Loan Bonds. (R. 33.)

SUMMARY OF POINTS DISCUSSED.

1. The only meaning, scope and effect of the Act is to establish, under the supervision of Federal officials, a system by which any owner of farm lands can borrow money thereon by a first mortgage repayable in a longer time and at a lower rate of interest than was previously possible—such result to be secured by a plan of collective mortgaging and by the exemption of the mortgages, notes and bonds from all forms of Federal and State taxation. (Infra, pp. 18-21.)

2. The Farm Loan Act so far as it creates Joint Stock Land Banks, is unconstitutional because Congress has no power to enable farmers to borrow money from the public at low interest rates; nor has it power, in order to accomplish such a result, to create a purely private corporation, and then, to exempt from State taxation (1) all farm mortgages executed to such a company, and (2) the obligations of such company (secured by the mortgages) when in the hands of the public. (Infra, pp. 21-71.)

3. The Farm Loan Act, so far as it creates Federal Land Banks, is unconstitutional, for the same reasons advanced with respect to the Joint Stock Banks; and its constitutionality is not saved as an alleged exercise of the Congressional power (1) to appropriate money, or (2) to borrow money on the credit of the United States. (Infra, pp. 72-.....)

FIRST POINT.

The only meaning, scope and effect of the Act is to establish, under the supervision of Federal officials, a system by which any owner of farm lands can borrow money thereon by a first mortgage repayable in a longer time and at a lower rate of interest than was previously possible—such result to be secured by a plan of collective mortgaging and by the exemption of the mortgages, notes and bonds from all forms of Federal and State taxation.

There is no dispute as to the meaning of the Act.

The language of the Act. It provides a system by which *any* person can mortgage his farm land to one or the other of two Federal corporations, who in turn can issue and sell to the public, their own obligations (Farm Loan Bonds) secured by such mortgage. The mortgages, bonds, and the income therefrom (and, in case of the Federal Land Banks, its capital, reserve, surplus, and the income therefrom) are then exempted from all State and other taxes. The accuracy of this statement of the Act will hardly be disputed.

*The intent of Congress and the Government's official announcements of the purpose and scope of the Act.** The Reports of Committees, the Debates, and the Governments' authorized announcements show, without qualification, that the *sole purpose* of Congress, and the *only object* sought to be obtained, was to provide a means by which the owners of farm lands might borrow money, on long time mortgages, at much lower rates of interest than they otherwise could obtain; and that this result was to be achieved principally by *exempting* the mortgages and bonds from every form of State and Federal taxation.

A number of extracts from the Reports, Debates and Announcements are collected in the Appendix.

In declaring the Federal Child Labor Law unconstitutional, this Court said (*Hammer* v. *Dagenhart,* 247 U. S. 251, 275):

*The debates and Reports of Committees may be resorted to not to vary, limit or broaden the construction of the language, but to advise the Court of the *intention* of Congress in order that such intention shall indicate the scope and purpose of the Act and the subject sought to be dealt with. (*U. S.* v. *St. Paul M. & M. Ry. Co.,* 247 U. S. 310, 318, and numerous cases there cited; *McLean* v. *U. S.,* 226 U. S. 374, 380; *Standard Oil Co.* v. *U. S.,* 221 U. S. 1, 50.)

> "A statute must be judged by its natural and reasonable effect. *Collins* v. *New Hampshire*, 171 U. S. 30, 33, 34."

The cases cited in the margin* establish the rule to be that the constitutionality of a statute must be determined by its effect and operation as manifested by the natural and reasonable meaning of the words employed; and by that rule the Act is simply one to establish a system of farm mortgages.

This is not a case where an Act, which on its face is rested upon some *undisputed* power of Congress is contested upon the ground (1) that a *wrongful purpose* actuated Congress to pass it in order to accomplish indirectly some end not within its constitutional power (*McCray* v. *U. S.*, 195 U. S. 27, 53-56; *In Re Kollock*, 165 U. S. 526, 536; *U. S.* v. *Doremus*, 249 U. S. 86, 93), or (2) that the result of the exercise of such lawful power produces injurious effects or interferes with some State power. (*Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 169.)

---

*(*Minnesota* v. *Barber*, 136 U. S. 313; *Yick Wo* v. *Hopkins*, 118 U. S. 356, 366; *Pure Oil Co.* v. *Minn.*, 248 U. S. 158; *Home Savings Bank* v. *Des Moines*, 205 U. S. 503, 510; *Lochner* v. *New York*, 198 U. S. 45, 60, 61, 64; *Dobbins* v. *Los Angeles*, 195 U. S. 223, 236; *Postal Telegraph Co.* v. *Taylor*, 192 U. S. 64, 73; *Bailey* v. *Ala.*, 219 U. S. 219, 238, 244; *Western Union* v. *Kansas*, 216 U. S. 1, 27-29; *Ludwig* v. *Western Union*, 216 U. S. 146, 162.)

The attack on the present Act asserts (*a*) that there is a total lack of power in Congress to deal with the subject matter, and (*b*) that this legislation bears no sort of relation to any power possessed by Congress.

SECOND POINT.

The Farm Loan Act so far as it creates Joint Stock Land Banks, is unconstitutional because Congress has no power to enable farmers to borrow money from the public at low interest rates; nor has it power, in order to accomplish such a result, to create a purely private corporation, and then, to exempt from State taxation (1) all farm mortgages executed to such a company, and (2) the obligations of such company (secured by the mortgages) when in the hands of the public.

In holding an Act of Congress unconstitutional (*U. S.* v. *Harris*, 106 U. S. 629, 636) this Court said that

> "Every valid Act of Congress must find in the Constitution some warrant for its passage";

and then quoting from Justice STORY, laid down the following rule for testing the validity of Congressional Acts:

> "Whenever, therefore, a question arises concerning the constitutionality of a particular power, the first question is whether the

> power be *expressed* in the Constitution. If it be, the question is decided."

There is no express power in the Constitution, authorizing Congress to create a corporation for the purpose of dealing in farm mortgages, lending money thereon, or issuing its own obligations secured thereby, or to exempt from State taxation, farm mortgages or the bonds of corporations.

The Court then continued,

> "If it be *not* expressed, the next inquiry must be whether it is properly an *incident* to an express power and necessary to its execution. If it be, then it may be exercised by Congress. If not, Congress cannot exercise it." (Citing many authorities).

To what express power of Congress is the creation of the Joint Stock Banks properly an incident? How is it an incident thereto or in anywise appropriate to the *execution* of such power?

I.

So far as the Joint Stock Banks and the Farm Loan Bonds issued by them are concerned, the Act provides that private persons, with private capital, may organize such a company, for private profit, in which the Government has no financial interest or representation (§ 16); that the company may lend on

farm mortgages; that all farm mortgages (and the income therefrom), executed to such a company shall be exempt from all State and Federal taxation; and that the obligations issued by the company (called Farm Loan Bonds) and the income therefrom, secured by such farm mortgages, shall also be wholly exempt from all taxation. (§ 26.)

In the case of the Joint Stock Banks, there is not even the flimsy pretense (which nominally exists in the case of the Federal Land Banks) that the power of appropriation is involved or that the money raised by the mortgages is to be used for agricultural development. There is *no limit or restriction whatever* as to the *purposes* for which the money loaned may be used, as Joint Stock Banks are expressly exempted from the limitations imposed upon Federal Land Banks in that respect. (Cf. § 16; § 12, Clause Fourth (*a*), (*b*), (*c*), (*d*).)*

*Even the co-operative and collective plan of borrowing by the farmers; the joint and several liability of the banks, and the full degree of Federal supervision, which exist in the case of the Federal Land Banks and were the strongest arguments advanced in Congress in favor of the Act, were specifically *dispensed with* in the case of the Joint Stock Banks, because some farmers might object to a co-operative undertaking with their neighbors, or to the publicity and scrutiny thereby entailed. (Senate Rep. 144, p. 11; House Rep. 630, p. 910; 1st Annual Rep. of Federal Farm Loan Board, p. 22.)

For example, an anarchist owning unimproved, vacant, uncultivated farm lands can mortgage them to a Joint Stock Bank in order to use the money to advance the cause of Bolshevism; and, yet, the mortgage, the income therefrom, the collateral trust bond (Farm Loan Bond) issued against it and secured thereby, and the income therefrom, are *wholly exempt* from all State and Federal taxation.

The banks are expressly prohibited from receiving deposits or doing any banking or other business (§ 16); or, as repeatedly stated in the Committees' Reports and in the Government's bulletins:

> "Joint Stock Land Banks are not permitted to engage in *any* business but making farm mortgage loans and issuing bonds" (64 Cong. 1st Sess. Senate Rep. 144, p. 11; House Doc. 494, p. 14; Report 630, p. 10).

and

> "These Joint Stock Land Banks are *private institutions* intended for the investment of *private capital*" (Farm Loan Primer, p. 15; Ed. July 23d, 1918).

The bill alleges, and the demurrer concedes, that private persons as shareholders own and operate the Joint Stock Banks purely and exclusively for their own individual and private

profit, as in the case of any other purely private corporation. (R. 5.) No Government money can, under any circumstances, ever be invested in any Farm Loan Bonds issued by Joint Stock Banks. (§ 6, 32; Act Jan. 18, 1918, 40 Stat. 431.)

The foregoing review demonstrates that the Joint Stock Banks are engaged exclusively in the ordinary private business of lending on farm mortgages and of selling to the investing public "collateral trust" bonds thereon, just as any private individual or State corporation might do; and that this business has no sort of public nature or connection with the Federal Government, but is of a wholly private character. The business does not in the remotest degree tend to carry into execution any express power of Congress; and hence no implied power exists in Congress to authorize the carrying on of this purely private business.

If this proposition should be disputed, then we ask *what* is the legitimate end within the scope of the Constitution to the accomplishment of which this purely private business is an appropriate means?

A moment's reflection will show that it is

impossible to indicate any of the objects entrusted to Congress by the Constitution which are in the remotest degree accomplished by the business of private individuals lending money to land owners on farm mortgages, and selling them to the public, which, after all, is the Joint Stock Land Banks' only business.

II.

The Government's argument in support of the Joint Stock Banks is this:

Congress has the power to create depositaries of public money and financial agents of the Government (*McCulloch* v. *Maryland,* 4 Wheat. 316; *Farmers &c Nat. Bk.* v. *Dearing,* 91 U. S. 29); it may also confer thereon the right to do a private business which otherwise would not be within the implied power of Congress. (*Osborn* v. *Bank,* 9 Wheat. 738, 864; *First National Bank* v. *Union Trust Co.,* 244 U. S. 416); and, from that premise the Government deduces the conclusion that because Congress (§ 6) authorized the Secretary of the Treasury to designate the Joint Stock Banks depositaries and financial agents, it was also entitled to confer upon them the right to con-

duct the private business of lending on farm mortgages.

As the Joint Stock Banks have never been designated, nor have they acted, as depositaries or financial agents (R. 5, 10), the Government's contention amounts to the assertion, that Congress *acquires the right* to create a corporation, to endow it with the power to do things which Congress has no right to regulate or control, and to exempt it from the power of the States, by the simple expedient of declaring that the Government may, *if it chooses,* use a corporation as its agent in some particular (but without ever so using it).

Such a claim of Congressional authority has never before been advanced in this Court and must be promptly rejected.

Congress does not have the power to create a corporation to engage in a purely private business which is beyond Congressional control by merely conferring upon it the potential power (which never has been, and may never be, exercised), to act for the Government, when such private business does not bear any possible relation toward promoting the potential power to perform a Federal service.

The numerous arguments that have been advanced in support of the Act, amount to the rough-and-ready claim that because Congress has the implied power to establish banks which *inter alia* deal with ordinary *commercial* credits, *consequently,* it must also have the right to establish banks to deal with *agricultural* credit; but the authors of those arguments, confused by the use of the term "Bank," have failed to appreciate the grounds upon which Congress is authorized to establish what they term a bank of commercial credit.

When the grounds upon which the power of Congress to establish the old Bank of the United States and the present National Banking System, are critically examined, it will be seen that the power to create such banks is rested upon circumstances wholly absent in the case of the Joint Stock Banks.

Both the First and the Second Banks of the United States and the present National Banks were created immediately after, or during, a great war, for the express purpose of affording the *means* for the *execution* of important *express* powers vested in Congress.

We submit,

I. The decisions in McCulloch v. *Maryland, Osborn* v. *Bank of U. S. and Farmers' Natl. Bank* v. *Dearing, do not afford any basis for the creation of the Joint Stock Banks.*

1. The Joint Stock Banks are expressly *prohibited* from doing every single thing which was held to be the constitutional basis for the incorporation of the First and Second Banks of the United States and of the National Banking System; while, on the other hand, the only thing the Joint Stock Banks are *permitted* to do (*i. e.,* lend on real estate mortgages) was expressly *prohibited* to both the Banks of the United States, and, until 1913, to all National Banks.

Therefore, the creation of the Joint Stock Banks (with but one function to perform and denied all others) cannot be based upon the arguments and considerations which justified the creation of the old Bank of the United States and the National Banks who were *prohibited* that *one* function and *given all the others?*

2. (*a*) The authorities cited in the margin* show that the First and Second Banks of the United States were in fact *the means actually used* by the Government to carry on its fiscal operations; to obtain loans in anticipation of revenues; to facilitate the payment of Federal taxes; to furnish a uniform and orderly currency on a sound specie basis; to collect, safeguard and transport money, and to transfer public funds from place to place (without cost to the Government or loss to it on account of the difference in exchange) as the exigencies of the Nation required.

The appropriateness, if not the absolute necessity for the Second Bank of the United States as a national agency, arose from the fact that there was an utter chaos in banking; the

*Bank of the United States. *McCulloch* v. *Maryland*, 4 Wheat. 316, 407-409; *Osborn* v. *Bank*, 9 Wheat. 738, 861-864; Beveridge's Life of John Marshall, Vol. 4, pp. 171, 176-195; Holdsworth & Dewey's "First and Second Banks of the United States"; McMaster's History of the People of the United States, Vol. 2, p. 29; Id. Vol. 4, p. 280 *et seq.*; especially pages 300-318; Hamilton's Report on a National Bank.

National Banking System. Lincoln's Veto Message of June 23, 1862 (6 Messages and Papers of the Presidents, pp. 87, 88); Lincoln's 2nd Annual Message, Dec. 1, 1862 (Id., pp. 126, 129-130); Rhodes' History of the United States, Vol. 4, pp. 237-239; Noyes' "History of the National Banking Currency," p. 41; Davis' "The Origin of the National Banking System," pp. 79, 80, 89, 106, 109; *Veazie Bank* v. *Fenno*, 8 Wall. 533, 536-539, 548.

Government had been deprived of its almost indispensable fiscal agent (the First Bank of the United States); the Government could not negotiate loans; taxes were collected with great difficulty, loss, and delay; the Treasury was so near bankrupt that the Department of State did not have sufficient money to pay its stationery bill; in desperation, the Treasury exchanged 6 per cent Government bonds for the notes of State Banks, thereby losing $5,000,000 from worthless bank bills. The local State Banks became the sole depositaries for Government funds, the worthless currency of such banks flooded the country, interfering with commerce and all business, while the suspension of specie payments by the State Banks rendered a uniform national currency indispensable.

(*b*) The National Banking System was established, and was *in fact used* by the Government, in order to furnish a sound and uniform currency and to prevent injurious fluctuations thereof; to facilitate the payment of troops, to receive subscriptions for, to distribute among the public, and to provide a market for, Government bonds which were used as the basis of the notes issued by the banks; to furnish de-

positaries at convenient places throughout the country for public funds, at a time when every collector of Federal taxes was afraid to deposit the money in State Banks, was responsible for the funds collected and yet was compelled to hold it in his personal possession, subject to the danger of fire and accident, as the Government did not even furnish an office safe for that purpose.*

(*c*) By what authority can Congress create a bank?

In *McCulloch* v. *Maryland,* 4 Wheat., 316, the implied power of Congress to incorporate a bank was based upon the ground that in order to carry out the *express* powers to collect taxes, to borrow money, to regulate commerce, to carry on war and to raise and support armies and navies, it was absolutely necessary for the Government to conduct fiscal operations; that a bank was a convenient, useful and essential instrument in the prosecution of fiscal operations and therefore Congress was authorized to create the bank and use it for those purposes.

In *Osborn* v. *Bank,* 9 Wheat., 738, the Court re-examined the basis of the *McCulloch* deci-

*For authorities, see footnote at p. 30, *supra.*

sion and reaffirmed it, holding (as the marginal authorities on p. 30, *supra*, demonstrate) that the Bank of the United States was not created for private purposes, but was created for National purposes only; that the operations of the Bank gave value to the currency in which all governmental transactions were conducted and acted as a machine for the money transactions of the Government; that "as a machine for the fiscal operations of the Government" it was *essential* for the Bank to engage in general banking business, as otherwise, the Bank could not perform these services for the Government which were exacted from it, and for which it was created.

Considering that the Bank of the United States was chartered by Congress for the *express purpose* of performing, and that it *did* perform, the indispensable governmental services necessary to carry into effect important, express and exclusive powers of Congress, how can it be contended that *those* decisions afford *any warrant* for Congress to create the Joint Stock Banks?

The basis of the *McCulloch* and *Osborn* cases was not even that the banks were mere passive depositaries or undefined financial agents, but

that by virtue of engaging in general banking, they were enabled to perform a great many active and indispensable services *essential* to be performed in order to carry on Government business.

In the case at bar, the Joint Stock Banks are expressly *prohibited* from doing those things which authorized the creation of the Bank of the United States. The private business of the Joint Stock Banks cannot in any conceivable manner serve as a means for carrying any Congressional powers into execution; nor do the Joint Stock Banks in fact perform any duties as depositaries or financial agents.*

If it should be suggested that the mere potential power to act as depositary and fiscal agent, *ipso facto* authorizes these institutions to carry on a purely private business, exempted from State control and taxation, then *a fortiori* there would be exempted from State control and taxation the numberless State Banks and Trust Companies which, by

*If, at some future time, the Joint Stock Banks should be designated by the Secretary of the Treasury as depositaries and financial agents, and should then perform services of that character to such an extent that their private business in farm mortgage lending was either an incident or necessary to the adequate performance of such governmental duties, a different question would be presented which it is not necessary now to consider.

the Second, Third and Fourth Liberty Bond Acts were not only *designated*, but in fact *acted* as "depositaries" and "fiscal agents" of the United States "in connection with the operations of selling and delivering any bonds, certificates of indebtedness or War Savings Certificates of the United States."

Certainly institutions which *in fact* act as depositaries and fiscal agents of the United States pursuant to express statutory authority, would be more clearly exempted from State taxation than a Joint Stock Bank which has a mere possibility in that direction, but which has never been vitalized by designation from the Secretary of the Treasury.

Since the passage of the Farm Loan Act, the United States has gone through the greatest war in history; its fiscal operations have exceeded many fold its previous combined operations since the beginning of the Government; it has called into service, as a means for carrying out its fiscal powers, innumerable agencies, individual and corporate, none of which were ever deemed to be thereby exempted from State taxation or control; and yet it is now solemnly argued that the Joint Stock Banks, engaged in a wholly private business, are ex-

empted, although they have never as yet been designated to act as depositaries or fiscal agents.

3. On the other hand, the *McCulloch* and *Osborn* cases are controlling authorities *against* the validity of the Joint Stock Banks.

In *McCulloch* v. *Maryland,* after holding that Congress could charter that particular bank because it was an appropriate means, plainly adapted to a legitimate end within the scope of the express powers granted by the Constitution, the CHIEF JUSTICE emphasized the fact that in order to justify the incorporation of a Bank it must be an *appropriate* measure to carry out *express* powers.

The Court said (p. 423):

> "Should Congress, *under the pretext of executing its powers,* pass laws for the accomplishment of objects *not* entrusted to the Government, it would become the painful duty of this tribunal should a case requiring such a decision come before it, to say that such an act was not the law of the land. But where the law is not prohibited, and is *really calculated* to effect any of the objects entrusted to the Government, to undertake here to inquire into the degree of its necessity, would be to pass the line which circumscribes the judicial department, and to tread on legislative ground."

In view of the debates of Congress, the Reports of the Committees, the official announcements of the Government, and the reasonable and natural effect of the language used in the acts, can anyone doubt that Congress undertook the accomplishment of an object not entrusted to it, namely, to provide a farm loan mortgage system throughout the States; and attempted to save its constitutionality by the pretext of declaring that the Secretary of the Treasury might designate the corporation a depositary and financial agent? If the present state of case does not fall directly within the above language of CHIEF JUSTICE MARSHALL, what case could fall within it?

Again, in *Osborn* v. *Bank*, the great Chief Justice, while sustaining the validity of the bank's creation, notwithstanding the fact that it engaged in private business while carrying out its governmental functions, emphasized the fact that the bank was created *primarily for national purposes* and that it was only necessary to allow it to do private business in order to effectively carry out the national purposes for which it was particularly created. In other words, in order to be an effective *means* for performing the fiscal operations of the

Government, it was desirable that the Bank should be engaged in the private banking business as well; because, for example, if the Bank collected public revenues and locked them up as in a subtreasury, the country would be unduly drained of currency with many resultant governmental disadvantages. (See, also, Lincoln's speech in reply to Douglas, December, 1839: Vol. 1, pp. 197-198 of Lincoln's Writings, Constitutional Edition.)

Continuing, the CHIEF JUSTICE said that if the Bank had been created "having private trade and private profit for its great end and principal object" it would have been taxable by the State (and do not the Joint Stock Banks have as their great end and principal object, private trade and private profit)—but that the Bank of the United States was *not* chartered principally for private profit, saying (p. 859):

> "This mere private corporation, engaged in its own business, with its own views, would certainly be subject to the taxing power of the State, as any individual would be; and the *casual circumstance* of its being employed by the Government in the transaction of its fiscal affairs would no more exempt its private business from the operation of that power than it would exempt the private busi-

ness of any individual employed in the same manner."

Does not that language precisely describe the Joint Stock Banks, except that they are not even *casually* employed by the Government, never having been designated by the Treasury Department for that service, and may never be?

Emphasizing that Congress could not create a corporation to carry on a private business, the Court declared that the Bank of the United States (as the history of the times demonstrates, p. 30, *supra*) was not chartered in order that private individuals might carry on the banking business, but that it was created especially as a means for executing the powers vested in Congress, saying (p. 860):

> "The Bank is not considered as a private corporation, whose principal object is individual trade and individual profit; but as a public corporation created for public and national purposes. That the mere business of banking is, in its own nature, a private business, and may be carried on by individuals or companies having no political connection with the Government, is admitted; but the Bank is not such an individual or company. It was not created for its own sake, or for private purposes. *It has never been supposed that Congress could create such a cor-*

poration. The whole opinion of the court in the case of *M'Culloch* v. *The State of Maryland* is founded on, and sustained by the idea that the Bank is an instrument which is 'necessary and proper for carrying into effect the powers vested in the Government of the United States.' It is not an instrument which the Government found ready made, and has supposed to be adapted to its purposes; but one which was *created,* in the form in which it now appears, for *national purposes only.*"

Will anyone have the hardihood to contend that the Joint Stock Banks were only created in order to enable Congress to carry out national purposes vested in it?

Referring to the Bank's power to transact private, as well as public, business, the Court said (p. 861):

"Why is it that Congress can incorporate or create a Bank? This question was answered in the case of *M'Culloch* v. *The State of Maryland.* It is an instrument which is 'necessary and proper' for carrying on the fiscal operations of government. *Can this instrument,* on any rational calculation, *effect its object unless it be endowed with that faculty of lending and dealing in money* which is conferred by its charter? If it can, if it be as competent to the purposes of government without as with this faculty, there will be much difficulty in sustaining that essential part of the charter. If it cannot, then

this faculty is necessary to the legitimate operations of government, and was constitutionally and rightfully engrafted on the institution."

Would not Joint Stock Banks be as competent to act as depositaries and financial agents of the government, *without* the added faculties of lending on farm mortgages, as *with* it?

The Court next decided that, as a matter of fact, it was necessary for the Bank, in performing its functions "as a machine for the money transactions of the Government" to "be endowed with that faculty of lending and dealing in money which is conferred by its charter" and in short, that the private trade of lending and dealing in money, was *necessary* to enable the Bank to perform the very services for which it was created.

The Farm Loan Act expressly prohibited the Joint Stock Banks from receiving deposits or transacting any banking or other business except that of lending on farm mortgages?

For what express national purposes were the Joint Stock Banks created? In what way is such national purpose dependent for its proper execution, upon the lending of A's money to B at low rates, and exempting its transactions

from State taxation? What fiscal operations of the Government are aided by the private business of farm mortgages? In what way is that branch of the business necessary to enable a Joint Stock Bank to perform any national purpose?

II. Osborn v. *Bank and 1st National Bank* v. *Union Trust Co. do not support the contention that Congress has the power to create the Joint Stock Banks for the purpose of engaging in the Farm Mortgage business.*

Remembering that the Joint Stock Banks are prohibited from doing any banking business and are confined to the business of farm mortgage lending, let us examine the *Osborn* and *Union Trust Co.* cases to see what bearing they have on the subject.

(*a*) In the *Osborn* case, as we have just seen, it was held that the business of general banking conducted for private profit, was, of and in itself, *essential* to be carried on, in order to furnish the necessary facilities that the corporation might in turn act "as a machine for the money transactions of the Government"; and for that reason alone, it was held that Congress had the right to endow the Bank

with ordinary banking functions as a necessary means for executing conceded powers of Congress. But certainly it cannot be contended that the farm mortgage business bears any relation whatever to the execution by the Joint Stock Banks of any express power of Congress, especially as the Joint Stock Banks have never been designated to act.

(*b*) Since the creation of the National Banking System, almost every State in the Union has passed laws to permit a corporation to exercise both commercial banking powers and *fiduciary* powers.

In 1913 Congress, by the Federal Reserve Act, authorized National Banks to exercise fiduciary powers.

In *First National Bank* v. *Union Trust Co.*, 244 U. S. 416, it was held that Congress had the constitutional power to endow national banks with the capacity to transact private fiduciary business. The decision was based upon the ground that while ordinarily it might be beyond the power of Congress to enter the fiduciary field, yet, as State banks had very generally taken on such powers and had thereby obtained an advantage over National

Banks, it was competent for Congress to give them these additional powers in order to make the operation of the National Banks successful.

The Court said the ruling in *Osborn* v. *Bank* was (p. 420):

> "that although a particular character of business might not be when isolatedly considered within the implied power of Congress,"

yet

> "if such business was appropriate or relevant to the banking business the implied power was to be tested by the right to create the bank and the authority to attach to it that which was relevant in the judgment of Congress to make the business of the bank successful."

That is exactly our explanation of the *Osborn* case (pp. 32, 33, 37, *supra*), namely, that in order to enable the Bank successfully to perform its functions as a machine for the fiscal operations of the Government, Congress could authorize it to conduct such private banking business as tended to make it a more effective Government agent.

The Court criticised the lower court because it had considered the power of Congress to enter the fiduciary field as an independent question and had not considered it as a neces-

sary incident to the performance of the Bank's governmental functions, saying (p. 424) that the lower court

> "instead of testing the existence of the implied power to grant the particular functions in question by considering the bank as created by Congress as an entity with all the functions and attributes conferred upon it, rested the determination as to such power upon a separation of the particular functions from the other attributes and functions of the bank and ascertained the existence of the implied authority to confer them by considering them as segregated, that is, by disregarding their relation to the bank as component parts of its operations—a doctrine, which, as we have seen, was in the most express terms held to be unsound in both of the cases [*McCulloch* v. *Maryland* and *Osborn* v. *Bank*]."

Again the Court said:

> "What those cases [*McCulloch* and *Osborn*] established was that although a business was of a private nature and subject to State regulation, if it was of such a character as to cause it to be incidental to the successful discharge, by a bank chartered by Congress, of its public functions, it was competent for Congress to give the bank the power to exercise such private business in co-operation with or as a part of its public authority. * * * From this it must also follow that even although a business be of such a charac-

> ter that it is not inherently considered susceptible of being included by Congress in the powers conferred on national banks, that rule would cease to apply if by state law state banking corporations, trust companies, or others which by reason of their business are rivals or *quasi*-rivals of national banks, are permitted to carry on such business."

Joint Stock Banks are not only *not* national banks, but are prohibited from doing everything that national banks are authorized to do.

Can it be successfully contended that because Congress uses National Banks as a means for the execution of conceded constitutional powers and may confer upon them private powers deemed necessary for the successful performance of their public duties, it is also competent for Congress primarily to confer such private powers upon a corporation which performs *no* public functions? Or, putting it in a slightly different way, can Congress assume the power to authorize corporations to enter upon fields of activity reserved to the States, by the simple declaration that such corporation *may*, at some future time, be used, not as National Banks are used, but as an incidental and unimportant governmental

agency wholly unrelated to the private business sought to be authorized? If Congress has that power, then this government ceases to be one of enumerated powers and Congress can enter upon any prohibited field of endeavor.

(*c*) As most State Banks are authorized to lend upon real estate mortgages, it was, of course, a mere matter of expediency whether Congress should authorize National Banks to enter that field; but that is because the National Banks are actually employed as the *means* of executing the express powers of Congress; and the addition of certain private powers falls clearly within the doctrine of the *Osborn* and *Union Trust Co.* cases. But it is a very different thing for Congress to enter primarily upon a prohibited field and endeavor to justify it, not even by employing the corporation as a Government agent, but by merely declaring that it shall have a possible power to act as such Government agent, without such power being actually exercised.

If the doctrine contended for by the Government be sound, is there any limit to the fields of private endeavor in which Congress may enter?

Before the Farm Loan Act was passed, National Banks had been given the power to lend on farm mortgages for terms of not exceeding five years. If Congress had thought it desirable to give National Banks the power to lend on farm mortgages for longer terms, no question of its constitutionality could probably be raised, as such a function was within the discretion of Congress to declare necessary to the performance of the bank's public duty. Such an exercise of discretion by Congress would probably be beyond judicial review, because, for many obvious reasons, Congress would be restrained from going beyond what was reasonably necessary or appropriate. But no such restraining influence protects the people from the encroachments of Congress if it may enter upon a prohibited field without the existence of an actual public agency to which such field is incidental.

III. The farm mortgages executed to the Joint Stock Banks and the Farm Loan Bonds issued by them and held by the general public, are subject to State taxation.

Since the argument below the Joint Stock Banks have been selling both the individual

farm mortgages to them as well as Farm Loan Bonds issued by them; and the frontispiece to this Brief illustrates the effect of the tax exemption, the value of which will be increased as States, like New York, seek to tax incomes for State purposes.

The States have unquestioned power to tax (1) mortgages and (2) corporate bonds or notes, held by their citizens or kept within their limits.*

The power to tax exists concurrently in both the State and Federal Governments; and is equally indispensable to the existence of each (*McCulloch* v. *Maryland*, 4 Wheat. 316, 425; *Lane Co.* v. *Oregon*, 7 Wall. 71, 76, 77).

The Constitution does not expressly prohibit the States from taxing the instrumentalities of the Federal Government, and contains no restriction whatever on the power of either to tax, except a few express prohibitions not here material**; nor does it grant any power

---

**Savings Society* v. *Multnomah Co.*, 169 U. S. 421, 426, 427, and cases there cited; *Kirtland* v. *Hotchkiss*, 100 U. S. 491, 498; *New Orleans* v. *Stempel*, 175 U. S. 309, 322; *Bristol* v. *Washington Co.*, 177 U. S. 133; *De Ganay* v. *Lederer*, 250 U. S. 376, 381, 382, and cases there cited.

***On Congress:* No tax on exports; direct taxes must be apportioned; indirect taxes must be uniform; *On the States:* No tax on exports; no tax on imports, except for inspection purposes; no duty on tonnage.

to Congress to exempt property from State taxation or otherwise to control State action as to taxes.

Nevertheless, by the Farm Loan Act Congress has attempted to deprive the States of the power to tax a species of property which has always been taxed and is one of the principal sources of revenue to many States, counties and cities.

Where does Congress obtain such a power? Certainly there is no *express* grant. Is there an implied power to exempt property from State taxation? If so, to what express power is it incidental?

The answer to these questions is that there are certain *implied* limitations on the taxing power of both the State and Federal Governments arising out of the very nature of our dual system of Government (*McCulloch* v. *Maryland,* 4 Wheat. 316, 425, 426; *The Collector* v. *Day,* 11 Wall. 113, 123; *U. S.* v. *Railroad Co.,* 17 Wall. 322, 327; *Railroad Co.* v. *Peniston,* 18 Wall. 5, 30; *Dobbins* v. *Commissioners,* 16 Pet. 435, 447; *Van Brocklin* v. *Tennessee,* 117 U. S. 151, 157 *et seq.*); that any restriction upon the State's power to tax arises from the operation of the Constitution itself;

and that Congress cannot, by any declaration of exemption, create one that would not have equally existed without such declaration. In other words, any attempt by Congress to exempt property from State taxation, if valid, is merely declaratory of what the exemption would have been anyway, without such declaration.

This leads us to consider the nature of the implied limitations on the taxing power, which have been consistently applied by this Court for just 100 years.

The doctrine was first announced by Chief Justice MARSHALL in *McCulloch* v. *Maryland;* and all subsequent cases have been applications of that principle, which has never been departed from, and of which the statutes are but declaratory.

Shortly after the Second Bank of the United States was incorporated for the express purpose of furnishing a means by which the fiscal operations of the Government might be conducted, numerous States endeavored to exterminate the Bank by the weapon of State taxation. At least eight States (Indiana, Maryland, Tennessee, Georgia, Illinois, North Caro-

lina, Kentucky and Ohio) passed laws which either directly prohibited the Bank from doing business within their limits, or imposed ruinous taxes upon it, or its branches, for the privilege of transacting business within the State, the taxes running as high as $50,000 or $60,000 a year upon each branch in Tennessee, Kentucky and Ohio (Beveridge's Marshall, Vol. IV, p. 207).

A Maryland Statute prohibited any Bank (other than Maryland State Banks) from issuing any notes except of certain specified denominations, which must be upon stamped paper, the amount of the stamps varying from $0.10 to $20, obtainable only from the State, in lieu of which a tax of $15,000 a year was imposed.

The validity of this statute as applied to the Bank of the United States, arose in *McCulloch* v. *Maryland*. After first holding, as heretofore pointed out, that Congress had the power to charter the Bank as a means of executing its fiscal operations, the Court held that a State could not tax the *means* employed by Congress to execute its powers; and this conclusion was based upon the ground that, as, the power to tax involved the power to destroy,

the States might so heavily tax the means or instruments employed by the Government in the execution of its national powers as to prevent the Government from functioning. Chief Justice MARSHALL stated his conclusions in the following language, which defines the implied limitation upon the taxing power of the States (4 Wheat. 436):

> "The Court has bestowed on this subject its most deliberate consideration. The result is a conviction that the States have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control the operations of the constitutional laws enacted by Congress to carry into execution the powers vested in the general government. This is, we think, the unavoidable consequence of that supremacy which the constitution has declared.
>
> We are unanimously of opinion that the law passed by the Legislature of Maryland, imposing a tax on the Bank of the United States, is unconstitutional and void.
>
> This opinion does not deprive the States of any resources which they originally possessed. It does not extend to a *tax paid by the real property* of the bank, in common with the other real property within the state, nor to a *tax imposed on the interest which the citizens of Maryland may hold in this institution,* in common with other property of the same description throughout the State.

> But this is a tax on the *operations* of the bank, and is, consequently, a tax on the operation of an instrument employed by the government of the Union to carry its powers into execution. Such a tax must be unconstitutional."

In *Osborn* v. *Bank* (involving the validity of an Ohio law passed "for the avowed purpose of expelling the Bank from the State" and imposing an annual tax of $100,000 as a privilege for doing business), it was held that as a matter of fact the private, as well as the public, operations of the Bank were *essential* to the performance of its services to the Government, and that a State could not tax it for the privilege of doing business.

In response to the contention of counsel (9 Wheat. 777, 794, 795) that in order for the Bank to be exempt from State taxation, Congress must insert a specific clause of exemption in the charter, the Court pointed out in the following language that the exemption from State taxation did not rest upon the exercise by Congress of any power to declare an exemption, but was incidental to the creation of the instrumentality itself and that the judicial power was the instrument to see that the necessary security of governmental instru-

mentalities from State Interference was obtained:

> "It is contended that, admitting Congress to possess the power, this *exemption* ought to have been *expressly asserted* in the act of incorporation; and, not being expressed, ought not to be implied by the court.
>
> It is not unusual for a legislative act to involve consequences which are not expressed. An officer, for example, is ordered to arrest an individual. It is not necessary, nor is it usual, to say that he shall not be punished for obeying this order. His security is implied in the order itself. It is no unusual thing for an act of Congress to imply, without expressing, this very exemption from State control which is said to be so objectionable in this instance. The collectors of the revenue, the carriers of the mail, the mint establishment, and all those institutions which are public in their nature, are examples in point. It has never been doubted that all who are employed in them are protected while in the line of duty; and yet this protection is not expressed in any act of Congress. It is incidental to, and is implied in, the several acts by which these institutions are created, and is secured to the individuals employed in them by the judicial power alone; that is, the judicial power is the instrument employed by the government in administering this security.
>
> That department has no will, in any case. If the sound construction of the act be that it

> exempts the trade of the Bank, as being essential to the character of a machine necessary to the fiscal operations of the government, from the control of the States, Courts are as much bound to give it that construction as if the exemption had been established in express terms."

This language has but one meaning and that is that when it comes to the exemption from State taxation of instrumentalities of the Federal Government in order that they may be preserved from destruction, it is at last the judicial power which must determine whether or not the exemption exists by virtue of the nature of the instrumentality.

The authorities show

First. That many means used by Congress as instrumentalities of the Federal Government have been subjected to the power of State taxation because, in the opinion of this Court, such taxation did not interfere with their operations for the Government.

Second. That such exemption exists not by virtue of any declaration by Congress that the exemption should exist, but under the Constitution *ex proprio vigore.*

Third. That in the case of the National

Banks, Congress has expressly provided (R. S. 5219) for the taxation of the shares of stock and the bank's real estate exactly as MARSHALL held in *McCulloch* v. *Maryland* they could be taxed.

A short review of the cases will show they are all consistent with these principles.

Means and Instrumentalities of the State and Federal Governments respectively exempted from taxation by the other. (*a*) It has been held that the States cannot tax Government bonds or other direct obligations of the United States (*Weston* v. *City of Charleston*, 2 Pet. 449; *Bank* v. *Supervisors*, 7 Wall. 26); nor bonds issued by municipalities in the Territories established by Congress for the Government of the people before their admission as States (*Farmers' Bank* v. *Minn.*, 232 U. S. 516) or by the District of Columbia (*Grether* v. *Wright*, 75 F. R. 742, 753, *et seq.*); nor land owned by the United States, either when purchased in pursuance of a governmental function, or acquired as a part of its territorial domain by a treaty or otherwise (*Van Brocklin* v. *Tenn.*, 117 U. S. 151); nor the receipts from coal mines owned by the In-

dians but operated by private parties under a lease from the Government in pursuance of the Government's treaty obligations to apply the revenues from the mines to the education of Indian children (*Choctaw & Gulf* v. *Harrison*, 235 U. S. 292); nor the salary of a Federal official (*Dobbins* v. *Commissioners*, 16 Pet. 435); nor the necessary operation of a means adopted by the United States to execute its express powers (*McCulloch* v. *Maryland*, 4 Wheat. 316; *Williams* v. *Talladega*, 226 U. S. 404, 418, 419); nor the franchise of a corporation created by Congress. (*California* v. *Pacific R. R. Co.*, 127 U. S. 1); nor the tangible or intangible property (except real estate) of corporations organized primarily as instrumentalities of the Government. (*Owensboro National Bank* v. *Owensboro*, 173 U. S. 664.)

(*b*) Similarly, Congress cannot tax the bonds or obligations of a State or its municipal subdivisions (*Pollock* v. *Farmers Loan & Trust Co.*, 157 U. S. 429, 584; *Mercantile Bank* v. *New York*, 121 U. S. 138, 162); or the salary of a State official (*Collector* v. *Day*, 11 Wall. 113, 124), or municipal revenues (*U. S.* v. *Railroad Co.*, 17 Wall. 322).

The principle underlying all of the foregoing cases, is that neither the State nor Federal Government can tax the property or operations of any instrumentality used by the other as a means of executing its powers, subject to the qualification (*a*) that such agent's real estate can be taxed (in common with other realty) and (*b*) that its other property can also be taxed in those cases where the agency is engaged in private business, which private business is not essential to the performance of its governmental duties.

The States tax the property and operations of persons and corporations engaged in private business, although also employed by the Federal Government in the transaction of its business. Accordingly, it has been held that a State can tax checks drawn by the United States in the payment of its interest obligations, notwithstanding an attempted Congressional exemption of United States obligations from State taxation. (*Hibernia Savings Society* v. *San Francisco,* 200 U. S. 310); the personalty, credits, money, etc., of a railroad company chartered by Congress, financially assisted by it, and engaged in performing Fed-

eral services (*Thomson* v. *Railroad*, 9 Wall. 579; *Railroad Co.* v. *Peniston*, 18 Wall. 5, 30-35; *Union Pacific* v. *Lincoln County*, 1 Dill. 314); while it is a matter of common knowledge that the States can tax and do tax many species of property which are being used by agents of the United States as the means of executing powers of the Government, such as telegraph lines, dredges, manufacturing plants (*Gromer* v. *Standard Dredging Co.*, 224 U. S. 362; *Baltimore Shipbuilding Co.* v. *Baltimore*, 195 U. S. 375, 382).

The reason why the States can tax the property and business of railroads, telegraph lines, etc., although they may have been chartered by Congress and used in part as governmental instrumentalities, and yet cannot similarly tax National Banks, lies in the following distinction between the two instrumentalities.

The railroads and telegraph lines could, in fact, perform all the services for the Federal Government just as well *without* the addition of private business, as they can with it (except as a money making proposition); and hence in accordance with the express language of *Os-*

born v. *Bank** the property and private operations of the companies are generally taxable by the State.

On the other hand, the banks, as pointed out in *McCulloch* v. *Maryland* and in the *Osborn* case, could only satisfactorily perform their Governmental duties by being endowed with the right to transact private business; as private banking business was the very thing which was needed to enable them to be an efficient machine for carrying out the money operations of the Government.

A Joint Stock Bank acting as a depositary, could, like the railroads, perform such a function just as satisfactorily to the Government without, as with, the addition of private business. That is an additional reason why the Joint Stock Banks fall as depositaries into the category of the railroads and not of that of the National Banks.

---

*The Court said (9 Wheat. 861) that there would be much difficulty in sustaining the private features of the Bank's charter "if it be as competent to the purposes of Government without as with this faculty" of transacting private business. But the Court held that the transaction of private business *was necessary* to the legitimate operations of the Government—not because it was more profitable to the Bank, but because the essential functions of the Government work could not be carried out so well, except in conjunction with private banking.

The mere possibility that at some future time the United States may elect to designate a Joint Stock Bank as a depositary and thereafter may further elect actually to use it as such, while in the meantime the corporation is engaged solely in private business for private gain, certainly does not constitute the corporation such an instrumentality of the Federal Government as to exempt it from State taxation.

In *Baltimore Ship Building Co.* v. *Baltimore,* 195 U. S. 375, 382, an old Government fort (of course not taxable) was conveyed to a shipbuilding company upon condition that it would construct a dry dock thereon, that the United States should have the right to use it forever free of charge, and that if its use as a dry dock was ever abandoned, the property should revert to the United States. It was held that the property was subject to State taxation, the Court saying:

> "It would be a very harsh doctrine that would deny the right of the States to tax lands because of a *mere possibility* that they might lapse to the United States. * * * Finally, we are of opinion that the land is not exempt as an agency of the United States. * * * The United States has no present

right to the land but merely a personal claim against the corporation, reinforced by a condition. But, furthermore, it seems to us extravagant to say that an independent private corporation for gain, created by a State, is exempt from State taxation either in its corporate person, or its property, because it is employed by the United States, even if the work for which it is employed is important and takes much of its time. *Thomson* v. *Pacific Railroad*, 9 Wall. 579; *Railroad Company* v. *Peniston*, 18 Wall. 5."

The fact that the company is chartered by Congress is not material (*R. R. Co.* v. *Peniston*, 18 Wall. 5, at p. 34).

At the argument below, it was suggested that because the Joint Stock Banks were given the power to buy and sell United States bonds (a power that practically every individual and corporation, State or Federal possesses), they thereby became instrumentalities of the Federal Government and exempt from State taxation. If that argument were sound, would not every corporation and person who had the power to invest in or who invested in Government securities, be exempted with respect to the *balance of their business* from State taxation?

This argument was considered and answered

in *Monroe Savings Bank* v. *City of Rochester*, 37 N. Y., 365, 370, in the following language, quoted with approval in *Plummer* v. *Coler*, 178 U. S., 115, 123:

> "It is, however, argued with great ingenuity and skill that, inasmuch as the plaintiffs, among other powers given them, have the right to invest their moneys in United States bonds, their franchises and privileges cannot be taxed by the State. The power thus to invest their money, it is contended, is a franchise for lending to the United States, and therefore cannot be taxed, because such taxation would trench on the power of the United States to borrow. This is stretching the argument too far. * * *
>
> The position, that a franchise granted by the bounty of the State is not taxable, because coupled with that franchise is the privilege of loaning money to the general Government, is not more untenable than to argue that, because such a franchise enhances the credit of the United States, therefore the Legislature could not repeal the law granting the franchise without violating its constitutional obligation."

The farm mortgages executed *to* the Joint Stock Banks as well as the Farm Loan Banks issued *by* them thereon, and held by private investors are exclusively instruments of private business.

Can it be contended that they partake in the slightest measure of the characteristics of those properties which have been held to be instrumentalities of the Federal Government and hence exempt from State taxation?

The Farm Loan bonds are neither assets nor liabilities of the United States. It does not promise to pay or guarantee the payment of them. No suit could be brought in the Court of Claims upon them. The money raised on the bonds does not go to the Government.

Congress cannot, by its mere declaration, exempt property from State taxation. The exemption, when it exists, arises from the operation of the Constitution upon our dual system of Government. If the Government's argument is sound that the mortgages and bonds are Federal instrumentalities, and thus exempt from State taxation, there is nothing to prevent Congress from destroying the State Governments by successive measures to withdraw from the States all species of property from taxation. That this is a legitimate test of constitutional power, see *South Carolina* v. *United States,* 199 U. S., 437, 454-455, where it was the principal argument for not exempting whisky from Federal taxation.

Congress is now considering the creation of a similar system of Federal *building loan banks* for the purpose of furnishing money at low rates of interest and on long term mortgages, to enable people to buy and build homes;

> The "indispensable essential of the system" being that "these bonds are to be tax exempt" "because the bonds can not be sold if they are to be subject to taxation," and "that will be doing no more than we did with the Federal Farm Loan Act with regard to mortgages taken by the Federal Land Banks," where "we called them instrumentalities of the Government." (See "Hearings before the Committee on Banking and Currency of the House of Representatives on H. R. 7597," pp. 7, 8.)

The advocates of the Bill avowed with perfect frankness (p. 11):

> "The United States Government is not expected to put 50 cents into this system; they are not called upon to finance it in any way, shape or manner, excepting to the extent of providing a supervision that will see that the system functions properly. *And to provide for tax exemption of their securities*, and, as I said before, * * * to be perfectly frank about it, *we feel that the tax exemption is an essential element of the system*, and in that connection we are justified in making this comparison, that if the Congress of the

> United States for any reason has seen fit to exempt the bonds of the Farm Loan System *for the purpose of giving easier and larger capital to the farmers* of the United States, we believe we are justified in calling attention to the fact that the *wage workers* of the cities, towns and villages of the United States * * * " (interrupted).

If the farmers and the home builders are entitled to get money at low rates of interest by exempting the loans and mortgages from State taxation, certainly the importance of manufactures, as shown in Alexander Hamilton's "Report on Manufactures" would fully justify Congress in providing a system of Federal Manufacturing Banks by which all mortgages and bonds on manufacturing establishments would be exempted from State taxation. This could readily be followed by a similar system with respect to irrigation projects, coal mines, logging, etc.; and if the Federal Government can exempt the bonds and mortgages from State taxation, can it not as readily exempt the land itself, for after all, in many States, a mortgage is an *interest* in land.

Again, if the Joint Stock Banks' possibility of performance of incidental Government duties, authorizes Congress to exempt its pri-

vate operations and assets from all taxation, then cannot Congress make *all* Banks potential depositaries, declare libraries the custodians of copyrighted books, department stores and drug stores agencies for the sale of War Savings Stamps, insurance companies agencies for the compilation of census statistics, and railroads, wagon roads, areoplane routes, etc., instrumentalities of interstate commerce and thus exempt from State taxation, everything connected with their private business profits.

Indeed, as a means for carrying into effect its express powers, Congress has already authorized steam railroads to carry Government troops, supplies, mails, etc.; has declared railroads, canals, etc., to be post roads; and has authorized State Banks and Trust Companies to act as both "depositaries" and "fiscal agents" of the Government in connection with the sale of Government bonds, certificates of indebtedness and War Savings Certificates. (See Second, Third and Fourth Liberty Bond Acts.)

Because State Banks and Trust Companies have been thus designated as depositaries and fiscal agents of the Government, and have in

fact served as such Government instrumentalities, can it be contended that Congress has the power to declare that all mortgages executed *to* such State institutions are Federal instrumentalities and exempt from State taxation; and that all collateral trust bonds issued *by* such State institutions (as vast numbers of them constantly do issue), are instrumentalities of the Federal Government and likewise exempt from State taxation?

It must be remembered that we are considering a question of *constitutional power.* If, as the Government now contends, Congress *has the power* to create a possible depositary and fiscal agent and can declare its private business and all obligations executed to or issued by it, exempt from taxation, certainly the principle supporting such action, also authorizes Congress to designate individuals, firms and corporations as depositaries and fiscal agents, and thereby exempt their private business from State taxation. There is no pretense that the private business of the Joint Stock Banks is (as in the *McCulloch* and *Osborn* cases), essential to the performance of governmental duties.

The shares of National Banks are exempt

from State taxation (unless permitted by Congress). If, then, these Joint Stock and Federal Land Banks are to be sustained on the principle of the National Banks, it would be within the control of Congress to exempt from State taxation the shares of stock in State corporations used as depositaries or fiscal agents, and also the property and business of firms and individuals similarly so employed.

For some years past State banks, trust companies, firms and private bankers have been the *means* by which Congress has collected income taxes at the source, thereby acting as important Federal instrumentalities in the execution of the express power of taxation. The income tax law requires all firms or corporations engaged in the business of collecting foreign payments of interest or dividends to be licensed by the Government and to withhold the income tax at the source. The fact that these persons were engaged in that foreign business made them peculiarly valuable as collecting instrumentalities of the Government's taxes. Could Congress have declared that mortgages executed by persons to such Banks, Trust Companies, firms or private

banking houses, were exempt from taxation and that all bonds issued by such institutions or persons were similarly exempt from taxation in the hands of third parties who purchased them as an investment?

THIRD POINT.

The Farm Loan Act, so far as it creates Federal Land Banks, is unconstitutional, for the same reasons advanced with respect to the Joint Stock Banks; and its constitutionality is not saved as an alleged exercise of the Congressional power (1) to appropriate money, or (2) to borrow money on the credit of the United States.

1. The argument as to Joint Stock Banks applies equally to the Federal Land Banks and need not be repeated, as the differences between the two classes of banks, as summarized in the margin, do not strengthen the constitutionality of the Federal Land Banks.

---

*The Federal Land Banks are restricted to loans (*a*) of not over $10,000, and in their own district (*b*) to actual farmers for purposes of farm improvement, to buy a farm, or to refund a pre-existing mortgage, (*c*) which are the collective liability of the group of borrowers organizing each farm loan association; and the Farm Loan Bonds issued thereon are the joint liability of all twelve banks.

On the other hand, Federal Land Banks can receive

2. The Government's principal argument in support of the Federal Land Banks is one which could not be made on behalf of the Joint Stock Banks. It is based upon the express power to tax and the power implied therefrom to appropriate money, and arises from the fact that the Government temporarily subscribed for most of the capital stock of the Federal Land Banks after the general public had refused to take it.* Before dealing with that contention it will be desirable to consider the nature and extent of Congress' power to tax and, consequently, to appropriate money.

---

*Since then the Government's stock has been considerably retired, *while the private shareholders have increased until they hold more than double the value* of the Government stock. The aggregate capital stock is about $20,000,000 of which the United States owns only about $8,000,000.

---

deposits from their own stockholders, the farm loan associations, which is an imaginary rather than a real function, as the borrowers are not likely to be making deposits on which no interest can be paid. (§ 13, Clause Sixth.) The Secretary of the Treasury may make limited deposits "for the temporary use of any Federal Land Bank"; and temporarily the United States owns most of the capital stock, which is being automatically retired so that the borrowers will shortly own all the stock.

Like the Joint Stock Banks the funds for the operation of the banks are furnished by the general public purchasing the Farm Loan Bonds which are secured by farm mortgages.

Art. 1, § 8, Clause 1, of the Constitution provides:

> "The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, *to pay the Debts and provide for the common Defense and general Welfare of the United States.*"

Although the subject of much discussion, it may be considered as settled that the italicized words did not confer on Congress any substantive power to provide for the country's general welfare, nor are they merely harmless introductory words limiting the subsequently enumerated powers.*

The accepted view is that Congress has power to lay and collect taxes *for the purpose of* paying the debts and providing for the common defense and general welfare, thereby

---

*(Federalist No. 41; Jefferson's "Opinion on the constitutionality of a National Bank," Feb'y 15, 1791; Jefferson's letter to Gallatin, June 16, 1817; Madison's veto of the Bonus Bill, March 3, 1817; Monroe's veto of the Cumberland Road Bill, and his *"Views of the President of the United States on the subject of Internal Improvements"* May 4, 1822; Madison's letter to Stevenson Nov. 17, 1830; 3 Farrand's Records of Federal Convention 483; Story on Constitution, §§ 907-930; 1 Willoughby on Constitution § 22; 1 Tucker on Constitution, §§ 222-223; 1 Hare's Am. Const. Law, 241-242; 1 Watson on Constitution 398; 10 Fed. Stat. Ann. 403 and authorities cited; *Van Brocklin* v. *Tennessee*, 117 U. S. 151, 158.)

qualifying the objects for which taxes may be laid.

Despite the powerful arguments of many statesmen, the views of Mr. HAMILTON, in his Report on Manufactures, have prevailed in actual practice, namely, that Congress can appropriate money raised by taxation for any purpose or object which it deems conducive to the *general* (as distinguished from *local*), welfare; and such action is almost, if not entirely, beyond the control of judicial power. While practically there are few, if any, limitations on the power of Congress to *appropriate* money, all the authorities are agreed that the power is exhausted upon the application of the money. Mr. HAMILTON, in his Report on Manufactures (December 5, 1791) said:

> "It is, therefore, of necessity, left to the discretion of the National Legislature to pronounce upon the objects which concern the general welfare, and for which, under that description, an appropriation of money is requisite and proper. And there seems to be no room for a doubt that whatever concerns the general interests of learning, of agriculture, of manufactures, and of commerce, are within the sphere of the national councils, *as far as regards an application of money.*

> • • • No objection ought to arise to this construction, from a supposition that it would imply a power to do whatever else should appear to Congress conducive to the general welfare. *A power to appropriate money* with this latitude, which is granted, too, in express terms, *would not carry a power to do any other thing* not authorized in the Constitution, either expressly or by fair implication."

President Monroe, in his "Views of the President of the United States on the Subject of Internal Improvements" accompanying his veto of the Cumberland Road Bill (which is universally conceded to be the most thorough and elaborate view which has ever been taken of the subject of Congress' power to appropriate money) was of the opinion that Congress could appropriate money to any purpose which it deemed conducive to the general welfare, *but that it could go no further than to appropriate the money* and could not undertake the projects to which the money was applied.

After disposing adversely of Mr. Madison's contention that the power of appropriation was limited to the execution of the powers enumerated or implied therefrom, Mr. Mon-

NOE said (II Messages and Papers of the Presidents, p. 167):

> "If, then, the right to raise and appropriate the public money is not restricted to the expenditures under the other specific grants according to a strict construction of their powers, respectively, is there *no limitation* to it? Have Congress a right to raise and appropriate the money to any and to every purpose according to their will and pleasure? They certainly have not."

He then argues that the money can be appropriated to any great national purpose including good roads, canals, foreign concerns, and says (p. 168):

> "The right of appropriation is nothing more than a right to apply the public money to this or that purpose. *It has no incidental power, nor does it draw after it any consequences of that kind.* All that Congress could do under it in the case of internal improvements would be to *appropriate* the money necessary to make them. For every act requiring legislative sanction or support, the State authority must be relied on. The condemnation of the land, if the proprietors should refuse to sell it, the establishment of turnpikes and tolls, and the protection of the work when finished must be done by the State. To these purposes the powers of the

General Government are believed to be utterly incompetent."

In his accompanying veto message Mr. Monroe said:

"A power *to establish* turnpikes with gates and tolls, and to enforce the collection of tolls by penalties, *implies a power* to adopt and execute a complete system of internal improvement. A right to impose duties to be paid by all persons passing a certain road, and on horses and carriages, as is done by this bill, involves the right to take the land from the proprietor on a valuation and to pass laws for the protection of the road from injuries, and if it exist as to one road it exists as to any other, and to as many roads as Congress may think proper to establish. A right to legislate for one of these purposes is a right to legislate for the others. It is a complete right of jurisdiction and sovereignty for all the purposes of internal improvement, *and not merely the right of applying money under the power vested in Congress to make appropriations*, under which power, with the consent of the States through which this road passes, the work was originally commenced, and has been so far executed. I am of opinion that Congress do not possess this power; that the States individually cannot grant it, *for although they may assent to the appropriation of money* within their limits for such purposes, they can grant no power

of jurisdiction or sovereignty by special compacts with the United States. This power can be granted only by an amendment to the Constitution and in the mode prescribed by it."

ANDREW JACKSON, in vetoing the Maysville Road Bill, said with reference to the appropriation of money. (Id., p. 488):

> "*No aid can be derived from the intervention of corporations.* The question regards the character of the work, not that of those by whom it is to be accomplished."

Mr. MADISON, in vetoing the Bonus Bill on March 3, 1817, said (Id., Vol. I, p. 584):

> "A restriction of the power 'to provide for the common defense and general welfare' to cases which are to be provided for *by the expenditure of money* would still leave within the legislative power of Congress all the great and most important measures of Government, *money* being the ordinary and necessary means of carrying them into execution."

In 1 Willoughby on the Constitution, it is said (Sec. 269):

> "In fact, however, the limitation that an appropriation should be for a public purpose has been without practical effect, as the courts have in no case attempted to hold invalid an appropriation by Congress on the

> ground that it has been for a purpose not public in character; and, as regards the restriction that appropriations shall be in aid of enterprises which the Federal Government is empowered to undertake, the doctrine has become an established one that Congress may *appropriate* money in aid of matters which the Federal Government is *not* constitutionally able to administer and regulate."

In 1 Hare's American Constitutional Law, pages 241-250, there is an admirable review of the whole subject, including many of the historic instances involving the appropriation of money by Congress. He points out that the construction of railways, high roads, bridges and other internal improvements is derivable, *not* from the power to *appropriate money,* but from the war, postal and commerce powers. Referring to certain appropriations it is said:

> "In the greater number of the instances above referred to, the government did not act in its sovereign capacity, *but like a rich and public-spirited individual who draws his pursestrings for the common good;* and therefore they do *not* tend to show that Congress may, by virtue of the eighth section of the first article, devise internal improvements and enact such laws as are necessary and proper to render the scheme effectual.

> It is one thing to construct a highway by virtue of the power of eminent domain, and exercise an absolute jurisdiction over it when made, *and another to lay out a road through land acquired by purchase* with the consent of the state through which it passes. So Congress may well be entitled to *appropriate money* for public education, or even to build and endow colleges and schools, *and yet want the right to make attendance compulsory and enforce it by fines or penalties.*"

It is also said:

> "IN OTHER WORDS, ALTHOUGH THE UNITED STATES MAY GO INTO THE MARKET AND DO WHATEVER CAN BE DONE BY THE USE OF MONEY WITHOUT THE EXERCISE OF LEGISLATIVE, EXECUTIVE, OR JUDICIAL POWER, THEY CANNOT, SPEAKING GENERALLY AND WHERE THERE ARE NO SPECIAL GROUNDS, DO MORE."

In Tucker on the Constitution, Vol. 2, §§ 222-234, there is elaborate consideration of the entire subject; and it is pointed out that if Congress, under the power of appropriation can supervise and intervene in the administration of the project to which the money is applied, our Government would be exercising a power not conferred upon it.

The extent of the power of appropriation has never been determined by this Court.

(*Field* v. *Clark*, 143 U. S., 649, 695; *U. S.* v. *Realty Co.*, 163 U. S., 427, 433.) But, for the purposes of this argument, we shall not question the right of Congress to appropriate public money to any purpose it may desire. We shall, however, insist that the implied power to *appropriate* for the general welfare is limited to the *disbursement* of money, with, at most, such machinery for its application to the desired end as may be used without the exercise of Federal power to abridge the rights of the States or the citizens thereof.

3. This brings us to consider

THE GOVERNMENT'S ARGUMENT AS FORMULATED BY HON. CHARLES E. HUGHES.

The Government contends that Agriculture is a matter of national concern; that whatever tends to assist or to develop it contributes to the "general welfare"; that the lending of money to farmers at low interest rates is an aid to the Agricultural interests; and, therefore, that Congress can appropriate money in order to lend it to farmers at low rates of interest.

The same principle would, of course, support

gifts, or loans, to manufacturers, to miners, to wage earners, to the salaried class, to the aged poor, to the unemployed, or to those engaged in educating the youth of the land; and it is at least debatable whether such favors to a limited class of citizens are really an aid to the subject of which they are representatives, or are for the "general welfare."

However, assuming, without conceding, that under the power of appropriation Congress can give or lend the public money to any class it desires, the question involved on this appeal is *not* as to the public money appropriated, nor the investment thereof, nor the power of Congress to make appropriations through the creation of corporations. The question is whether Congress can *exempt* from State taxation and control,—not its own money so appropriated, *but the private capital of private investors loaned on farm mortgages as an ordinary business investment.*

The Government's argument is reducible to a series of propositions, each representing a supposed implied power of Congress claimed to be logically deducible from a preceding power, and is substantially as follows:

I. That the power of appropriation implies the right to select any proper means for making the appropriation effective; that the creation of corporations is a proper means; that the $9,000,000 temporary subscription by Congress to the capital stock of such corporations is a legitimate means by which to lend public money to farmers at low rates of interest; that Congress can endow the corporation not merely with what is necessary to carry out the appropriation itself, but also with such private powers for private profit as Congress may deem it desirable to confer; that the corporations so formed are instrumentalities of the Federal government for carrying out Federal purposes; that, as such, neither the property nor the operations of such corporations can be taxed by the States; that all mortgages executed to, and all bonds issued by, such corporations, *and held by private investors,* are instrumentalities of the Federal government, and exempt from State taxation.

II. That under the power to borrow money, the Farm Loan Bonds are exempt from State taxation, notwithstanding the fact that they are neither assets nor liabilities of the United

States, are not issued on the credit of the United States, and that its interest in the capital stock of the federal land banks is only temporary, is being rapidly retired, and has already been far exceeded by the private capital recently subscribed to the banks.

We submit:

I. The implied power of appropriation does not authorize the creation of Federal Land Banks to lend private capital on farm mortgages, nor the exemption of its obligations in private hands from State taxation.

1. Never before in our constitutional history has it been suggested that the power to create a corporation could be deduced from the power of appropriating public money. The United States subscribed largely to the capital stock of both the First and Second Banks of the United States. But neither HAMILTON, WEBSTER nor MARSHALL suggested that the creation of the Bank could be sustained under the power of appropriation, which was then, as here, exercised by a subscription to the Bank's capital stock; although, in the case of both

Banks of the United States, the Government's subscription was absolute and permanent, whereas here it was *conditioned* on the public not subscribing for the stock, and *temporary*, as it is now in the process of rapid retirement. If the Government's argument were valid, would it not have occurred to some of those great minds?

The fact that the power of appropriation has never been relied on to support the authority of Congress to create a corporation, or to do anything not justifiable under some other grant of power, is persuasive evidence that the *power of appropriation* cannot authorize the creation of these corporations.

2. If a corporation is created to engage in any activity, whether it be the construction or operation of railroads, the manufacture of ordnance or explosives, the building of a merchant marine, the improvement of navigable rivers, or the business of banking, the implied power to create it must arise from some express power conferred upon Congress, such as to tax, to declare war, to regulate commerce, etc. Possibly the power to appropriate money can be exercised through the creation of a corporation *to carry out the appropriation*, but that

does not give the right to authorize the company to engage in forms of activity other than appropriating the public money, nor to afford a medium for the investment of purely private capital in private enterprises, such as farm mortgages.

If a corporation may be the means by which appropriated money is disbursed, surely it cannot be used for the purpose of enabling private individuals to lend their money to other private individuals. It will always be borne in mind that we are dealing strictly with the power of appropriation and not with those powers upon which the National Banking System was founded and for the beneficial accomplishment of which it was necessary to permit the banks to engage in private business. (See pages 31, 32, *supra.*) The power to create ordinary banks was not based on the power to appropriate money nor to provide for the general welfare, but was based upon the necessity of carrying on the fiscal operations of the government in exercise of its powers to tax, to declare war, etc. How can it be said that the creation of a corporation for the employment of private capital in the farm mortgage business is plainly adapted or really calculated to effect

the appropriation of the small amount of money which the government has subscribed to the capital stock?

In *McCulloch* v. *Maryland*, it was said, page 423:

> "Should Congress *under the pretext of executing its powers* pass laws for *the accomplishment of objects not intrusted to the Government* it would become the painful duty of this tribunal * * * to say that such an act was not the law of the land."

Under the *pretext* of executing its power to appropriate money is not Congress seeking to create a machine by which one class of citizens can lend money to other citizens and be exempted from the operations of State laws with respect thereto? The money-lending business was never intrusted to the Government.

In *Osborn* v. *Bank*, 9 Wheat., 738, at 861, it was distinctly held that if the Bank could carry out the purposes of the Government as competently *without* the right to do private business, as it could *with* such right, there would be great difficulty in sustaining the private features of the charter. Certainly a corporation organized for the purpose of carrying out the *appropriation* of public money

could do so *without* the addition of the private business of farm mortgage lending.

3. Adopting the rule of *First National Bank* v. *Union Trust Co.*, 244 U. S., 416, 424, that the existence of the implied power to grant the function of private business must be tested, not by a separation of the different functions and by disregarding their relation to the bank as a whole, but by considering the bank as an entity, with all the functions and attributes conferred upon it, we find that the Federal Land Banks are agencies for the lending of money on farm mortgages; that the Government appropriated but a trifling amount; that private individuals have, within two years, contributed forty times that amount, and that in a short time the government's appropriation will have been returned to it, and the size of the private investment, now three hundred millions, will increase indefinitely, until it may reach the four billions now invested in farm mortgages.

4. Besides agriculture, there are many other subjects of national concern, such as the problems of personal morality; education of children, insurance of lives against death, disability and disease; the protection of property

from fire; the conservation of natural resources; the alleviation of poverty; and the relations between society and organized labor—all of them are matters of internal policy exclusively reserved to the States.

If Congress, under the power of appropriation, temporarily exercised to a limited amount, can create a great system of private money lending, let us consider to what extent the power may be carried.

Life and Fire Insurance. Certainly the protection of property against fire and lives against death is a matter affecting everyone. By a small temporary appropriation to capital stock, can Congress acquire the power to create gigantic life and fire insurance companies in which private capital can find investment, where the corporation will furnish money to persons suffering losses from fire or death, in return for low premium rates? Would all the immense capital thus invested, and the payments received from the members and the investments thereof be exempted from State taxation? Would payments made by the corporation for death and fire losses, also be exempted from taxation including inheritance taxes?

At the argument below the Government insisted that the Farm Loan Banks did not regulate any matter reserved to the States, but only related to the *application of money*. It will be observed that such an insurance corporation is purely a *financial* one, doing nothing except to *receive and disburse* money.

Conservation of natural resources. The conservation and development of coal, timber, water power, etc., are matters of great concern directly affecting the general welfare. Can Congress by small, temporary subscriptions to capital stock, authorize the creation of a "Conservation and Development Bank" to be engaged in the business of lending money at low rates to persons owning coal and timber lands, water power rights, etc., taking mortgages therefor and issuing its collateral bonds against them, which mortgages and bonds, as well as the huge private investment, shall be exempt from all State taxation? Could Congress, without appropriating any money, also authorize private capital to organize Joint Stock companies to engage in the same business, exempting the bonds and mortgages from taxation?

Irrigation of Arid Lands. The irrigation of arid lands is a public purpose (*Fallbrook Irrigation Dist.* v. *Bradley*, 164 U. S. 112; *Hauck* v. *Little River Dist.*, 239 U. S. 254). Could Congress, in order to stimulate the irrigation of arid lands (not public lands), authorize the creation of two classes of Irrigation Banks, one to which Congress would make a small temporary subscription for capital stock, and the other wholly organized by private individuals? And could it authorize those Banks to issue irrigation bonds secured by mortgages upon the proposed irrigated lands, which mortgages and the bonds should be exempt from State taxation? If so, what would become of the principles on which *Kansas* v. *Colorado*, 206 U. S. 46, 87-89, was based?

Education. Everyone will admit that education no less than agriculture is a matter of national concern and welfare. Could Congress, by a similar temporary appropriation for capital stock, authorize the creation of a corporation for the purpose of furnishing money to promote the cause of universal education, authorized to lend money at low rates to all persons building or operating school houses, colleges, technical or profession

schools, securing the money by mortgages on the plants and on the tuition fees of the students? Could Congress exempt such bonds and mortgages from State taxation? Could Congress have authorized Mr. Carnegie, Mr. Rockefeller and their associates to create a joint stock company with hundreds of millions of capital to be loaned or otherwise expended in assisting persons engaged in educational work and to withdraw from State taxation all such funds, together with the mortgages executed by the educators in return for the loans?

Child Labor. Congress cannot regulate child labor. (*Hammer* v. *Dagenhart,* 247 U. S. 251.) Can Congress, under the power of appropriation, create a corporation in which private capital would have the principal investment, for the purpose of discouraging child labor in factories, by lending money at low rates of interest to those factories who would refuse to employ child labor? Could Congress exempt from State taxation the loans thus made and the mortgages thus taken and the bonds issued against them? If so, the Congressional appropriation soon being returned to Congress (as the farm loan appropriation is being returned) we would shortly

have huge mortgage lending companies assisting factories all of whose operations and investments would be exempt from State taxation.

Suppression of Vice and Elimination of Venereal Disease. Congress has no power to suppress Houses of Ill Fame. (*Keller* v. *United States,* 213 U. S. 138.*)

Can Congress, by the same expedient of a trifling appropriation, permit Mr. Rockefeller and his associates to organize a corporation having for its object the suppression of vice and the elimination of venereal disease, by means of loans at low rates, or bounties paid, to immoral people in order to assist them in abandoning their vicious careers and getting a new start in life?

Would the capital thus invested, the loans taken from the unfortunate people, and the bonds issued thereon be exempted from State taxation?

Poverty and Unemployment. The development of the agricultural interests does not more greatly affect the general welfare nor is it a more important public purpose, than the

*Except, of course, under the war power. *McKinley* v. *United States,* 249 U. S. 297.

alleviation of poverty and unemployment. By the same system of appropriation, can Congress authorize philanthropists to organize corporations by which immense sums of private capital may be devoted to loans to the poor or unemployed, either without security or secured by chattel mortgages, assignments of salaries, or future earnings, etc? Could Congress exempt from State taxation the capital thus invested and the notes taken?

Public Disasters. In the case of a Chicago fire or a San Francisco earthquake Congress could doubtless (1) appropriate public money for the benefit of those whose property was destroyed, and (2) administer appropriate relief through the medium of a corporation whose capital was subscribed by the Government, but could it provide that private individuals (*a*) might take stock in the corporation, and (*b*) also organize an independent corporation wholly owned by such private individuals; and that the two corporations thus organized could lend money for the rebuilding of the destroyed districts, take mortgages therefor, issue collateral bonds against them, all of which should be exempted from State taxation?

We do not suggest any limitation upon the

power of Congress voluntarily to apply Federal money to the aid of any situation which Congress deems it wise to assist, but our criticism is that under that power of appropriation Congress cannot authorize private individuals to embark upon the same business and exempt them from the powers of the States, where such business bears no substantial relation to the execution of some Federal power.

II. The power to borrow money on the credit of the United States does not authorize the issuance and sale of Farm Loan Bonds to Private Investors, nor the exemption thereof from State taxation.

Congress has the power

> "To borrow money on the credit of the United States."*

1. Farm Loan Bonds do not represent the exercise of any power by Congress to borrow money on the credit of the United States. Con-

*It is probable that money so borrowed can only be applied in the execution of the *enumerated powers* of Congress, and those *implied* therefrom; that *borrowed* money cannot be applied for the "general welfare." and, therefore, the *borrowing* clause cannot be relied on in order to furnish money for the general welfare. Furthermore, all money borrowed should first be placed in the treasury and then appropriated by law. (Constitution, Art. I, § 9, clause 7.)

gress has not borrowed the money. The money is not borrowed on the credit of the United States. No money realized from the sale of the bonds is placed in the United States Treasury. None of the proceeds belong in any way to the United States. The disposition thereof is not made by Congress but by the directors of the Federal Land Banks who are not public officials. Farm Loan Bonds are neither an asset nor a liability of the government.

Congress voted down an amendment to guarantee the bonds, which shows that it did not intend to be considered responsible therefor. (*United States* v. *Del. & Hudson R. R. Co.*, 213 U. S., 366, 414.) The Government disclaims any liability on the bonds (Farm Loan Primer, Ans. 102).

Mr. CARTER GLASS said in the debate that the Government "took a very limited temporary stake in the system"; that he did *not* consider the Farm Loan system a government "instrumentality"; and that he disagreed with Mr. Hughes' opinion that the Government was morally bound on the bonds.

2. Money obtained from private investors by the sale to them of bonds issued by the Federal Land Banks and secured by the farm

mortgages of private farmers, is not money borrowed on the credit of the United States; and is not an exercise of the Congressional power to borrow money.

In response to the Government's argument that the bonds were executed under the borrowing power because the Federal Land Banks were chartered by Congress and a portion of the stock therein was owned by the United States, it is sufficient to say:

(*a*) The argument is an example of reasoning in a circle because in one breath the validity of the bonds is based on the borrowing power *because* executed by a Federal corporation, and, next, the very *existence* of the Federal corporation is defended as a *means* for executing the borrowing power.

(*b*) Congress has chartered several railroads, but no one has ever suggested that their bonds were valid under the borrowing power of the Constitution.

(*c*) Although the Farm Loan Bonds are issued by banks in which the United States was temporarily the principal stockholders (is now a *minority* stockholder and soon will be *no* stockholder at all), they were issued solely by

the banks upon the faith and credit of the mortgages pledged to secure their payment, and of the joint and several liability of the various land banks, who, by statute, are expressly made liable for the payment of the bonds. The Government's ownership of stock in the banks does not make the act of the corporation that of the government. (*Briscoe* v. *Bank of Kentucky,* 11 Peters, 257; *Bank of the U. S.* v. *Planters' Bank,* 9 Wheat., 904, 907; *Woodruff* v. *Trapnall,* 10 How., 190, 205; *Curran* v. *Arkansas,* 15 How., 304, 308-9; *Bank of Kentucky* v. *Wister,* 2 Peters, 318, 322; *Louisville R. R. Co.* v. *Letson,* 2 How., 497, 550.)

In short, the temporary ownership by the United States of stock in the Federal Land Banks cannot make the acts of the banks, the acts of the United States. Even in the case of The First and Second Banks of the United States, in which the Government was a large stockholder, and which were incorporated solely for the purpose of carrying out the express powers of Congress, it was held that none of the privileges of the Government were imparted to the Bank, but that the Government by becoming a stockholder, laid down its sovereignty so far

as respects the transaction of the corporation. (*Bank of the United States* v. *Planters' Bank, supra.*)

(*d*) The power of the States over liquor and the liquor traffic is absolute.* When, in order to lessen the evils of intoxication, South Carolina took over the liquor traffic and prohibited all sales except those made by itself through a system of dispensaries, this Court held that the whiskey was still subject to a Federal tax, because when a State, even in the exercise of its police power, engages in ordinary private business, the business is not exempted from the Federal taxing power because it is conducted by a State; and that the exemption of State instrumentalities from Federal taxation is limited to those of a strictly governmental character, and does not extend to those used by the State in carrying on an ordinary private business.

It is not necessary to extend this brief by lengthy quotations from Mr. JUSTICE BREWER'S opinion, with which the court is perfectly familiar. It is sufficient to observe that he

*Bartmeyer v. Iowa, 18 Wall., 129; Beer Co. v. Mass., 97 U. S., 623; Kidd v. Pearson, 128 U. S., 1; Crane v. Campbell, 245 U. S., 304; Barber v. Georgia, 249 U. S., 254.

pointed out the large and growing movement in the country in favor of State management of public utilities, including gas, water, and railroads; that the States might take over tobacco, oleomargarine or all businesses, and that if, by doing so, it could exempt the subjects taken over, from Federal taxation, the National government would be crippled. The same argument applies here. If Congress can withdraw from State taxation the whole field of farm mortgages, it can do the same as to real estate, manufacturing plants, public utilities, mines, private residences, etc.

As pointed out by CHIEF JUSTICE MARSHALL in the *McCulloch* case, reaffirmed in the *South Carolina* case, this is not a case for confidence by one government that the other will not exercise its power of exemption to its fullest extent. The States are entitled here, and now, to insist that Congress shall not drive an entering wedge by exempting farm mortgages, and the private investments based thereon, from State taxation.

In *Flint* v. *Stone Tracy Co.*, 220 U. S., 171, 173, where it was held that the States could not

withdraw from the Federal taxing power, corporations of a public nature, it was said:

> "It is no part of the essential governmental functions of a state to provide means of transportation, supply artificial light, water and the like. These objects are often accomplished through the medium of private corporations, and though the public may derive a benefit from such operations, the companies carrying on such enterprises are, nevertheless, private companies, whose business is prosecuted for private emolument and advantage. For the purpose of taxation they stand upon the same footing as other private corporations upon which special franchises have been conferred. The true distinction is between the attempted taxation of those operations of the states essential to the execution of its governmental functions, and which the state can only do itself, and those activities which are of a private character."

Certainly, it is no part of the essential governmental functions of the Federal government to provide farmers with money at interest rates lower than they can obtain in the open market. No matter what indirect benefit the public may derive from farmer prosperity, the companies conferring such prosperity are nevertheless private corporations whose business cannot be exempted from State taxation.

(*e*) The Farm Loan Act requires that an insignificant portion of the banks' capital (apparently 5 per cent of 25 per cent, *i. e.*, 1¼ per cent) shall be invested in United States bonds (Sec. 5). Obviously such a provision as to the capital stock affords no authority for the creation of the farm loan system and its exemption from State taxation.

(*f*) In this connection it must be remembered that the creation of the Joint Stock Banks cannot be based upon any ownership by the Government of its stock, or upon the exercise of the borrowing power, or upon any compulsory investment of its capital in Government bonds, because *none* of those elements exists with respect to the *Joint Stock* banks.

CONCLUSION.

In its last analysis, the questions to be determined are (1) whether the Constitution has endowed Congress with the power to provide for schemes of agricultural, social or industrial improvement calling for the use of large quantities of private capital; and (2) whether Congress, in its desire to see such schemes successfully realized, can infringe upon the

taxing power of the States by exempting therefrom the private capital so provided, thereby furnishing the desired scheme with money at a lower rate of interest, and on more favorable terms, than could otherwise have been secured.

If the principles announced in *Kansas* v. *Colorado* and *South Carolina* v. *United States* are still the law, it is inconceivable that Congress has the power to provide this system of farm mortgage banks, not for the purpose, as in the case of the National Banks or the old Bank of the United States, of carrying out some of the express powers of Congress, nor to enable Federal agencies adequately to perform their functions in view of the new forms of competition (*First National Bank* v. *Union Trust Co.*), but solely for the avowed purpose of enabling farmers to borrow money at low rates, because Congress thinks that people with capital *ought* to be willing to lend it on farm security, as cheaply as they lend it on, what the owners of the capital consider, a *safer* form of security.

Undoubtedly farmers have not been able to borrow money at as low rates as well established commercial interests, but this arises

from the very nature of the security offered by the farmers. In *Hammer* v. *Dagenhart* it was pointed out that the Constitution did not give Congress any authority to equalize economic conditions by which business done in one State was at a disadvantage compared with that done in another; so, Congress has no authority to equalize economic conditions, between two classes of citizens, with respect to the ability to borrow money from private sources.

If, in order to stimulate agriculture, Congress desires, under its power of appropriation, to lend the public money to farmers at a low rate of interest and easy terms, it is probable that the courts cannot control such action, but the ballot box would quickly stop it.

When, however, Congress, under the alleged guise of the power of appropriation, attempts to accomplish the same result through private capital, *at the expense of the taxing powers of the States*, then, in the language of *Hammer* v. *Dagenhart*:

> "This court has no more important function than that which devolves upon it the obligation to preserve inviolate the constitutional limitations upon the exercise of authority, federal and state, to the end that each may continue to discharge, harmoniously

with the other, the duties intrusted to it by the Constitution."

FRANK HAGERMAN,
WM. MARSHALL BULLITT,
Counsel for Appellant.

LOUISVILLE, KY., January 1, 1920.

APPENDIX.

The following extracts from the Reports of the Committees in Congress, the debates, and the Government's official announcements under the Act, all show that the sole and only purpose of the Act and object sought to be attained, were to give the farmers long-time loans on farm mortgages at *low* interest rates.

In introducing the bill originally, the Joint Committee reported as follows (53 Cong. Rec., 453, 489; 64th Cong., 1 Sess; Senate Report No. 144 and House Doc. No. 494):

> "* * * This bill *enables the farmer to obtain capital* for productive purposes, *at low rates* and for long terms, on the security of his farm. * * *
>
> The American Farmer does not come to Congress with a hard-luck story. He does not ask the Government to bestow on him the public money that all the people have contributed in taxes. He does not demand that the Government become a banker in order to borrow money on bonds and loan the proceeds to him. He merely calls attention to the fact that farming has become a business demanding large amounts of capital; he points out the undoubted excellence of the security he offers; and he demands legislation that shall put it in the power of those who are inter-

ested, and those who have money to invest, to extend to him the credit he requires. He desires the Government to authorize a system of land banks which shall duplicate for him the facilities now commanded by men engaged in manufacturing, in transportation, and in commerce. * * *

Of money seeking long-term investment at low rates there is an abundant supply. It includes the ordinary savings of the school-teacher, clerk, minister, and wage earner; the proceeds of life insurance in the hands of widows and other beneficiaries; funds belonging to estates, minors, and wards in chancery in the hands of executors, guardians, and trustees; funds of insurance companies, benevolent orders, and societies of various kinds; endowment of colleges, hospitals, museums, and other institutions; and assets to be invested by receivers, courts, and governments. The aggregate of these is enormous. They require an investment that is absolutely safe and reasonably liquid in the sense that it may be converted into cash upon moderate notice; in other words, that it may find a ready market. A safe investment of this character need not carry a high rate of interest. Here we discover the funds that should be made available to the farmer on long-term mortgage.

We may picture the owners of this vast wealth grouped on one side of a river, the farmers desiring loans grouped on the other

side. It is evident that each has what the other wants.

We are asked to furnish the bridge which shall bring them in touch, or rather to grant a franchise to those who will build the bridge if we will construct the approaches. *Such we conceive to be a proper function of the Government.* * * *

It is believed that the system of land banks outlined in the proposed bill affords a safe and attractive farm loan bond for the *investing public; low interest rates,* long term mortgages, and *easy payments* for the farmers; low cost of administration; simplicity of organization and operation; adaptability to the needs of every section; and stimulation to the spirit of generous co-operation among farmers."

The House Committee on Banking and Currency said (64th Cong. 1 Sess.; Report No. 630, p. 2):

"The *immediate purpose of this bill* is to afford those who are engaged in farming or who desire to engage in that occupation a vastly greater volume of land credit *on more favorable terms* and at *materially lower* and more nearly uniform *interest rates* than at present available."

"The means whereby this purpose is to be accomplished is provided through the establishment of national-chartered and Government-supervised organizations to grant long-time, amortizable loans at *low interest rates*

upon farm-mortgage security; to assemble in each organization individual farm mortgages into one collective security; and to issue upon this collective security credit instruments to be known as farm-loan bonds of such safety and soundness as to command the investment funds of the country in abundance." * * *

"In stating that the *immediate purpose* of the bill is to secure greater credit accommodation for the farmer the committee has had in mind the capital requirements of the farmer. Although the fact has been until recently almost entirely ignored, it is true that agriculture is a business as much as manufacturing or commerce is a business. With the rapid increase in population and the accompanying rapid rise in land value it has become more and more necessary that successful farming shall be conducted as a business. Modern agriculture needs and demands capital in constantly increasing volume." * * *

"A new form of credit instrument is created—the farm-loan bond. This bond is issued upon the capital of the land bank and the collective security of first mortgages. Every precaution has been taken to make it an absolutely safe form of investment. These bonds are sold to investors and the funds obtained are loaned to the farmer borrowers." * * *

"It is from the sale of Farm Loan Bonds that the Land Banks will be enabled to secure the funds to loan to the farmer."

In the course of the debate, Senator ROBINSON said, May 2, 1916 (53 Cong. Rec., 7228):

> "The *primary purpose* of this legislation is to secure long time loans at *low rates of interest* to those, who, under the terms of the Act, may avail themselves of its provisions."

Senator CUMMINS said (Id., p. 7246):

> "The *chief purpose* of the corporation as avowed by all who have spoken in its behalf, and, as I think will be admitted by everybody, is to secure a *lower rate of interest* to those who borrow from the Land Banks; *that is its only object.*"

The father of the bill, Senator HOLLIS, said (p. 6793):

> "If I did not believe that the bill would give the farmer a *lower rate* than he is now getting, I should not think it would be worth while to pass the bill. It is because we feel the farmer is not now getting loans at as *low a rate* as he is entitled to that we are passing the bill. If it has that result, I shall feel that we have *achieved our object.*"

The Government's official announcements of the purpose and scope of the Act. The Farm Loan Act (§3) requires the Government to issue from time to time official publications "setting forth the principal features of this Act and * * * the merits and advantages of farm loan bonds."

Accordingly the Treasury Department has issued a number of circulars and reports from which the following extracts are taken.

Circular No. 1 (March 20, 1917):

"These associations are organized for the *primary purpose* of giving to each borrower the benefit of the combined credit of all its members to the extent of the capital contributed and the limited liability they each incur, and hence the associations are required to endorse every loan made to members."

Circular No. 2 (March 20, 1917):

"What the Farm Loan Act promises.

Farmers want cheaper money. They ought to have it. The Federal Farm Loan Act aids them to get it. * * * The Federal Farm Loan Act *provides a way* of getting mortgage loans for farmers at *low rates* of interest, at lengths of time to suit the borrower and on *easy terms* of repayment. * * *"

Circular No. 3 (February 9, 1917):

"The law is a great new agency for furnishing money to finance the business of farming."

The Farm Loan Primer (p. 3):

"Q. What are the *general purposes* of the Federal Farm Act?

Ans. To *lower* and equalize interest rates on first mortgage farm loans; to provide long term loans with the privilege of repayment in installments through a long or short period

of years at the borrower's option; to assemble the farm credits of the Nation, to be used as security for money to be employed in farm development; to stimulate co-operative action among farmers; *to check land monopoly by making it easier for tenants to get land;* and to provide safe and sound long term investments for the thrifty."

First Annual Report of the Federal Farm Loan Board:

"* * * the Federal Farm Loan Act was enacted to create an institution which would furnish farmers with money at a *reasonable rate* and not be run on a profit producing basis" (p. 13).

"In order to provide capital for agricultural development at the *lowest possible rate of interest,* which was, of course, the *primary purpose* of the Act, it was essential," etc. (p. 17).

"The *general purpose* of the Act was to provide for the farm loan needs of the country" (22).

FARM LOAN CASE.

In the Supreme Court of the United States

October Term, 1920.

No. 199.

CHARLES E. SMITH, *Appellant,*

vs.

KANSAS CITY TITLE & TRUST COMPANY ET AL., *Appellees.*

Appeal from the District Court of the United States for the Western Division of the Western District of Missouri.

APPELLANT'S REVISED BRIEF.

WM. MARSHALL BULLITT,
FRANK HAGERMAN,
Solicitors for Appellant.

SMITH-GROVES LAW PRINTING, KANSAS CITY, MO.

INDEX.

Table of Cases Cited.

In the Supreme Court of the United States

October Term, 1920.

No. 199.

CHARLES E. SMITH, *Appellant,*

vs.

KANSAS CITY TITLE & TRUST COMPANY ET AL., *Appellees.*

APPELLANT'S REVISED BRIEF.

STATEMENT.

1. The general nature of the case.

This is an appeal (Rec. 3) from a decree (Rec. 30) below dismissing a bill (Rec. 1-19) filed to test the constitutionality of the various provisions of the Federal Farm Loan Act of July 17, 1916, as amended on January 18, 1918 (8 Fed. Stat. Ann. Supp. 1918, pp. 14-42; 39 Stats. L. 360; 40 Stat. L. 431). The United States (Rec. 30, 31,

34) and the Federal Land Bank of Wichita, Kansas (Rec. 20, 30, 31, 34), and the First Joint Stock Land Bank of Chicago, Illinois (Rec. 19, 30, 31, 34), representing the *two* classes of banks named in the Act, all *voluntarily* became parties, took practical charge of the defense (Rec. 31) and are now here for the second time, as appellees, seeking to obtain a speedy decision *on the merits* of *all* questions raised as to the validity of said Act and its tax exemption features.

On January 8, 1920, the case was *on its merits*, orally and in print, fully argued by Ex-Justice Hughes for the Land Banks and by Ex-Attorney General Wickersham for the Joint Stock Banks. In the brief of the latter Ex-Secretary McAdoo joined. He also filed for the United States an additional elaborate printed argument on the merits, signed by him as a special assistant to the Attorney General of the United States. On April 26, 1920, the court, after having had the case under advisement for over three months, restored it to the docket for re-argument. Here, this brief for appellant is filed as a new and complete one and as a substitute for those heretofore presented by him.

2. The proceedings below and the appeal.

Appellant, plaintiff below, is a large stockholder in the appellee, defendant below, which is a corporation organized as a trust company under the laws of Missouri (Revised Statutes Missouri 1909, Chap. 12, Arts. I, II and III; Laws of Missouri 1915, pp. 103-127, amending same; sec. 127, subd.

11, p. 167; Laws Mo. 1915, pp. 165-167), which provide:

> "Corporations may be created * * * for any one or more of the following purposes: * * * 11. To buy, *invest* in and sell all kinds of government, state, municipal and other bonds, and all kinds of negotiable and non-negotiable paper, stocks or other *investment securities.*"

A trust company is thereby authorized to *invest* its corporate and trust funds in such bonds as, in the eyes of the law, are *real* legal "investments," as distinguished from those which are unauthorized and pretended. The statutory power to deal in bonds is only "to buy, invest in and sell all kinds of government, state, municipal and *other* bonds and all kinds of negotiable and non-negotiable paper, stocks or *other* investment securities." These last words necessarily imply that any outlay of funds for securities which are not "investments" is illegal, unauthorized and *ultra vires.* So it was held by Circuit Judge Thayer in *Bierce* v. *Guardian Trust Company,* in an unreported opinion, a copy of which was attached to the brief on the first hearing, entitled "Appellant's Brief," as Part 1 of the Appendix, p. 81. Investments within this view do not, as he said, include bonds or stocks of any corporation which are of a speculative or other doubtful nature (17 A. & E. Enc. L., 2d Ed., 438, 440, 443, 444; *Lamar* v. *Micou,* 112 U. S. 452), and cannot be made in *illegal* bonds issued by an *illegal* organization under an unconstitutional statute (*id.*) be-

cause (*Norton* v. *Shelby Co.*, 118 U. S. 425) "an unconstitutional act is not a law, it confers no rights, it imposes no duties, it affords no protection, it creates no office; it is in legal contemplation as inoperative as though it had never been passed."

If a corporate fiduciary, as defendant is, wished to make an investment in securities of such character, it might have absolutely protected itself by applying to and obtaining from a court specific directions in the premises, the courts "having large powers of supervision over the investment of funds held by fiduciaries" (17 A. & E. Enc. L., 2d Ed., 431). If appellee would not, in this way, even ask any relief, manifestly a good faith protesting stockholder can, in the absence of its *voluntary* action, have an injunction against a proposed improper and illegal venture. Such was the theory of the bill. The course of this case shows, and all interested therein, including appellees' eminent counsel, now concede the propriety thereof. In its most simplified form, the case presented was one where the directors of the corporate defendant, over the objections and protests of the stockholding plaintiff, proposed and threatened to *invest* its corporate and trust funds in bonds issued under the Farm Loan Act, *not only* by the Federal Land Banks, but *also* by the Joint Stock Land Banks. Thereupon plaintiff filed his bill (Rec. 1-18) to enjoin as illegal and *ultra vires* each proposed and threatened action. The claim was that the Act (8 Fed. Stat. Ann. Supp. 1918, pp. 14-42; 39 Stat. L. 360; 40 Stat. L. 431) and the tax exemption (secs. 21, 26) features thereof were un-

constitutional and, hence, the bonds of *neither* bank were *real* "investments." The case has grown into one of great proportions and of national importance. The government, as well as each of the defendant banks, recognized that *all* questions as to the validity of the Act authorizing the bonds and all tax exemption features thereof were thereby fairly and satisfactorily presented. They *voluntarily* came into the case, assumed charge of the defense, presented, *on the merits*, the sole constitutional question involved and convinced the court below that it should uphold (Opinion, Rec. 22-30) the Act. The bill, so as to more fully present the case, was, *at the suggestion of the Government and these banks*, in certain unnecessary respects, amended (Rec. 34) by interlineation. Thereupon defendant filed a motion to dismiss (Rec. 31) because, *as thus amended*, it did not state facts sufficient to constitute a cause of action. The United States, through Ex-Secretary McAdoo, to whose activities the friends of the Act owe so much, appeared (Rec. 30, 31, 33, 34) *amicus curiae*. Both banks, agencies established by the Act, upon their intervention (Rec. 19, 20, 30, 31, 34), became parties defendant. They and the United States were permitted (Rec. 31) to and did "adopt as their own and were heard upon the motion to dismiss." This motion was sustained and a decree (Rec. 30, 31) entered dismissing the cause. Thereupon an appeal (Rec. 31) was allowed and the case brought here (Rec. 32-36), where all formalities were waived. Upon stipulation (Rec. 33, 34) it was advanced and is now here for final presentation, where it should

be, without question, determined on its merits (*Brushaber* v. *Union Pacific R. Co.*, 240 U. S. 1, 9, 10; Argument, Div. I).

3. Questions involved are the validity of the Farm Loan Act and its tax exemption features.

The sole questions involved are whether that which, by its terms, is designated as the Farm Loan Act (39 Stat. L. 360; 40 Stat. L. 431), establishing *each* class of banks, and its sweeping tax exemption features (secs. 21, 26) are violative of some express or implied provision of the Constitution.

4. Genesis of the Act.

In 1913, a three months' European summer trip, commonly called a junket, was taken by a United States commission composed of Congressmen of one political faith, and by a number of delegates appointed by the Southern Commercial Congress, a voluntary convention or association of citizens. (64th Congress, Senate Document 500, p. 29.) The latter was headed by one David Lubin, who was described as a "delegate of the United States International Institute of Agriculture, Rome, Italy," whatever that may mean. In a speech before the Commission Mr. Lubin (63d Congress, 1st Session, Sen. Doc. 114, p. 4) declared that the members thereof and the delegates were "at the feet of the German people to learn." A propaganda was afterwards started in Congress for the establishment in this country of a system of

rural credits, based upon the German plan of collective and co-operative borrowing and lending of money on long-time farm mortgages. The words "German plan" are used advisedly. Such plan was first adopted in Prussia. It found its principal development in Germany. Some modifications thereof have, however, been adopted and are in operation in other parts of Europe. It is quite significant that the plan is European, as the real question here is whether there *has, by Congress,* been enacted a law inimical to the spirit of our institutions, contrary to the provisions of our Constitution and in defiance of the reserved rights of the states and of the people. The commissions, ignoring the distinction between *federal* and *state* powers, confessedly, studied only European (not American) conditions and obtained a large amount of data about foreign methods. They came home enthusiastic about the German land mortgage scheme. Then followed extended public addresses, reports and discussions (63d Cong. 1st Sess., Sen. Docs. 17 and 214; 2d Sess., Sen. Docs. 261 and 380; 64th Cong. 1st Sess., House Doc. 494, House Rep. 630, Sen. Doc. 472; 64th Cong. 1st Sess., Sen. Doc. 9; 63d Cong. 1st Sess., Sen. Doc. 114; same session hearings on Rural Credits before House Sub. Com. of Com. on Banking and Currency and Joint Hearings on Rural Credits, before Subcommittees of Senate and House Committees on Banking and Currency). The most prominent characteristic thereof was the constant citation of German methods as an argument for our adoption of something of the same kind. A fair sample is found in an address (64th Cong.

1st Sess., Sen. Doc. 9, p. 21) of Senator Sheppard, of Texas, before the Texas Farmers' Congress on August 3, 1915, devoted to a glorification of German methods, a plea for their imitation here, and an argument that the nearer the American people approach the German system, "the more successful we will be." Merely because the system is German or of foreign origin does not *necessarily* imply that it is illegal. There may or may not be some excellencies in all or any of the various European plans. Such plans may be adaptable to foreign conditions, where class discriminations may be made and the right of local authorities to control and tax private property may be denied. The real inquiry is whether they can be adopted, ***not by the states,*** but by the United States, where totally different conditions prevail and constitutional limitations exist. The Act was approved (39 Stat. L. 360) July 17, 1916. This, however, was *before the war.* Hence, no exercise of a war power is involved, and any such thought may be dismissed. The nearest the war got to the scheme was that the government, under the amendment of January 18, 1918 (40 Stat. L. 431), *temporarily* loaned, for its support, money presumably extracted from the people for war purposes. The *main* purpose of the Act was, in fact (Argument, Div. IV) and as a matter of law, not to appropriate public money (*id.*, Div. VI), or have performed any substantial governmental function (*id.* Div. V), but, as always has been claimed by its most ardent supporter (*id.* Div. IV), *solely* to give, by *private* means, the farm owners, ***as distinguished from all others,***

money upon "easy terms," or, as put by the then Secretary of the Treasury, Mr. McAdoo, "*long*-term mortgages at *low* rates of interest," with a provision for repayment of the principal in annual installments, "so that the small *farmer*" to the exclusion of all others, could borrow and pay off both principal and interest "through annual installments which will be less than the straight interest charges he has been paying on his mortgages under the old system." To find a ready market for these loans, wholly *private* in their nature, they and all the *private* capital invested therein were attempted to be wholly withdrawn from *all* state control and taxation. The organizations charged with the execution of the Act were merely commission loan agents, and in an attempt to accomplish the desired result, were glibly miscalled *"banks"* and *"instrumentalities of the government."* As this case presents the question whether, under our system of government, the law is valid, there must be herein a determination of, *not* what the agencies (Federal Land Banks or Joint Stock Land Banks) appointed to carry out the Act are called, *but what they really are.* Put in still more concise form, the real question, regardless of the use of mere words, is whether the *main* purpose of the establishment of these *alleged* banks was to have exercised the *governmental* power of the nation, as distinguished from those powers respecting *private and proprietary* rights, which, however and by whomsoever owned, arise solely out of and adhere in the ownership and control of *private* property.

5. Passage and theory of the Act.

(a) The advocates of the scheme and their adherents had framed and passed the Farm Loan Act. It was based upon and passed by Congress with the seeming thought that although the Tenth Amendment to the Constitution reserved to the states all the powers not granted to the United States (and none were so granted as to a Farm Loan Act), yet since *general* banking was a *governmental* function, there was *implied* the power to establish such agencies, *calling* them Federal Land Banks and Joint Stock Land Banks, just as had been *implied* the power to establish national banks.

(b) The lawmakers evidently overlooked the thought which prompts this appeal, that it was not permissible for them to organize an institution not "of a *governmental,*" but mainly, if not entirely, "of a *private* character," ignore the difference between the scope and character of *"governmental"* and *"private* powers," and treat the latter as a wholly immaterial consideration. So, agencies were provided, the *main* purpose of which was to exercise merely private powers. They were *called* "banks" and "instrumentalities of the government," though nothing could have been further from the fact.

(c) Congress passed the Act, not as an appropriation, but on the alternative theory (Argument, Div. IV, subd. 2d) that either lending *private* money to farmers was "a proper function of government" (53 Cong. Rec. 453, 489), or that it was authorized so to do if, as Senator Cummins said

(53 Cong. Rec. 7246), *any* governmental functions, *no matter how "small or insignificant,"* were possible to be, *at any time,* performed by the agencies.

(d) The validity of the Act is, however, here, by counsel, sought to be (Argument, Div. III, subds. [a], [b]) upheld upon these two *conflicting* grounds: The Joint Stock Banks, through Ex-Secretary McAdoo and Ex-Attorney General Wickersham, contend that the agencies were created to perform governmental functions, and therefore the very power to create the government implied the power to create the agencies through which it was to function. The Land Banks, through Ex-Justice Hughes, practically contend that this theory is entirely wrong by claiming that the sole power is only found under the right of the government to appropriate public money for the general welfare of the people. Congress in passing the Act had no thought that such was the power which existed (Argument, Div. III). The doctrine is one that cannot be invoked in behalf of the Joint Stock Banks, for as to them there was no appropriation. No supporter of the Act thought that there was an exercise of the power to appropriate money. But *after* its passage an opinion of Ex-Justice Hughes was, by bond sellers, sought as to the validity of the Land Bank bonds. This opinion thus found the power, notwithstanding such position, if sustained destroyed the very existence of the Joint Stock Banks.

6. The substance of the Act, which was the attempted exercise by Congress of the power now challenged.

This case involves the sole question of the validity of the Farm Loan Act as amended (8 Fed. Stats. Ann. Supp. 1918, pp. 14-42; 39 Stat. L. 360; 40 Stat. L. 431), and its tax exemption features (secs. 21, 26) as applied to *both* the Land and Joint Stock Banks. The nature and character of the Act was, immediately after its passage, thoroughly dissected by students of the subject. Myron T. Herrick (119 Atlantic Monthly., p. 222, February, 1917), Charles A. Enslow (10 Lawyer and Banker, October, 1917, p. 402) and Allen Ripley Foote (The Injustice of the Federal Farm Loan Law, published by the American Progress Publishing Company, 145 East State Street, Columbus, Ohio) wrote articles of great force and interest. These may be consulted with profit. They not only explain the nature of the law, but conclusively show that the functions to be exercised by the newly created agencies were strictly *private*. They also show that there had been an *abortive* attempt to forever exempt from taxation Farm Loan bonds and mortgages, which attempt, if upheld, would deprive the states of those *internal* rights to which it has been here (Argument, Div. II) repeatedly decided they were justly entitled.

The *substance* of the Act is a scheme, the *main* purpose of which is to create, for borrowers and lenders, *private* corporate borrowing and lending *agencies*. In its most concrete form, the scheme

created and classified the agencies into corporations *called* Farm Associations, Land Banks and Joint Stock Banks. There was no limit either to the time of their existence or to the amount which could be loaned to borrowers on farm mortgages or to the bonds which could be issued and sold by the banks. The energies of these perpetual agencies were *exclusively* confined to lending on *farm* mortgages (1) through the Land Banks, with the aid of the Farm Associations, $10,000 or less to actual cultivators of the soil, with which to buy or improve the land, and (2) through the Joint Stock Banks, without any aid of the Farm Associations, *unlimited* sums to *any* person for *any* purpose whatsoever. The *alleged* banks were, however, only such in *name*. They did (Bill, Rec. 10) and could do no banking business (secs. 13, 14, 16). They are, however, of such *distinct* kinds that the *separate* nature of each should be kept distinctly in mind.

(1) *Farm Associations and Land Banks.*

Each of any ten or more cultivators and owners of farm lands may mortgage same for not more than $10,000, but *only to buy or improve them.* They must, however, *first* form a corporation, known as a Farm Association. This corporation, made up exclusively of borrowers, acts as a broker or commission agent ordinarily does, simply as a borrower's agency. In so doing, it indorses the paper of each borrower, thus, in a way, putting all borrowers behind each loan. Each borrower subscribes and pays for his stock in a sum equaling 5 per cent of the loan. This sum is

added to the mortgage and made part of the loan. The Farm Association must, however, apply to and obtain the money for the loan from a Land Bank, and, as a condition of so doing, must take and pay for exactly the same amount of the bank's stock. Thus the borrower in effect advances the capital of the Land Bank. The real parties to each loan are the borrower and the lender. They are, regardless of the agencies intervening, the only ones interested. One furnishes the money, the other pays it back with interest. In this the *public* has no concern, and the exercise of no *governmental* function is *essential.*

It is true that the *first* money to be loaned the borrowing farmers was obtained from the government by it subscribing and paying for about $750,000 of each Land Bank's stock. While it was to so take the stock, it was to be repaid therefor without interest and it could receive no dividends thereon. Each transaction was, therefore, practically a government *temporary* loan, without interest. Moreover, this kind of a loan, though by the government, relates (Argument, Div. V, subd. 2d) to a *proprietary*, not a *governmental*, interest. As business justifies it, the *government* Land Bank stock must be taken over with the money paid in by future borrowers in payment of their Farm Association stock subscriptions. The Land Bank, out of the first moneys, thus *temporarily* loaned, acquires farm loans. It then can, and is expected to, raise forever *new* money for *future* investment by the sale of its own collateral trust bonds secured thereby. This is the extent of its office, and it is strictly a matter of

private concern, if there is a distinction (Argument, Div. V, subd. 4th) between one which is *private* and *proprietary* and one which is *governmental*. When the Farm Association has taken up the government's *temporary* loan, held in the form of Land Bank stock, the government's interest, in a scheme supposedly permanent, absolutely ceases. The borrowers then, through their Farm Associations, become sole owners of the agencies and step into absolute control thereof. From that time the government has not even a *proprietary* interest. Yet the agency remains as a fully chartered institution performing no office for the United States.

(2) *Joint Stock Banks.*

Abandoning all the subtle reasons advanced for the use of the Land Banks, Congress, as an evident after-thought, conceived the notion of having established Joint Stock Banks. Had these been provided for in the original framing of the bill, Land Banks and Farm Associations would have been unnecessary, and nine-tenths of it could have been dispensed with. The government has not the slightest connection with the Joint Stock Banks, and can never have any interest therein, nor in the mortgages taken or bonds issued by them. The Farm Associations are not connected therewith. Individuals, not necessarily borrowers, *only* can organize, own and control same. These *alleged* banks can, independently of the Farm Association, loan to *anyone* on farm lands, in *unlimited* amounts and without any restrictions as to the use made of the land or to be made of the

money borrowed thereon. The extent of their calling is to lend directly on *farm* mortgages and issue and sell their own bonds with the mortgages as collateral trust security.

(3) *Difference between the Land and Joint Stock Banks.*

Not only is there a difference between the Land and the Joint Stock Banks as to the ownership and control thereof, but, in the case of the Land Banks, the loans are made to *farm* occupants in *restricted* amounts and for *specific* purposes, while with the Joint Stock Banks there is no aid from the Farm Associations, and there are no restrictions as to amount, persons or purposes. While in this way non-cultivating farmers or even speculators can borrow on vacant land and on easy terms, the large investor really reaps the *greatest* benefit, for he, by a *private* investment of *private* funds, is permitted to go absolutely tax-free. This benefit can last *forever* and reach untold sums, for there is neither limit of time in the existence of the banks nor in the amount of money that can be loaned to borrowers or to the amount of bank bonds which can be issued. This feature caused a learned writer (119 Atlantic Monthly 222, 232, February, 1917) to remark that "Congress ought, at least, to have specified the total that could be made."

(4) *Inducements held out to investors.*

To induce investors to *continue* to furnish, after the temporary government loan, the money for the Land Bank and *start* into that of the Joint Stock

Bank, a *huge* price is paid, if tax exemption can be considered a "price," as it actually is. The securities are a valuable form of *private* taxable investment (*Farmers & Mechanics Savings Bank* v. *Minnesota*, 232 U. S. 516, 521). Yet they are entirely and forever withdrawn from the domain of the states and arbitrarily made exempt from any kind of taxation, state or federal, by simply, but falsely, *calling* them "instrumentalities of the government." This short method of depriving a state of its revenue, if carried far enough, can destroy the existence of any local government. The discrimination against borrowers, not owning farms, and in favor of *large* investors and *farm owners*, is unfair and really so harsh and arbitrary as to be against the spirit of American institutions.

(5) *Land Banks may possibly be designated as government depositaries.*

All Land Banks *may*, by the Secretary of the Treasury, *be designated* as depositaries of public money, excepting receipts from customs. They *may* also be employed as financial agents of the government (sec. 6). They must in these capacities perform only such reasonable duties as *may* be *required* of them. (*id.*) These are mere minor *possibilities*, and at most are incidents to, not the *main* purposes of, the scheme. As hereafter shown (Argument, Div. V, subd. 5th, 6th), this provision was adopted as a mere device and subterfuge. This is apparent, for it was, as stated by no less a personage than Senator Cummins (53 Cong. Rec. 7246) deemed "necessary,

however, to find *some* governmental purpose, however *slight or insignificant*, in order to invoke the authority of Congress in the incorporation." Neither kind of agency has been, *as yet*, designated as such a depositary, nor, except in the specific instances about to be mentioned, been employed as such a financial agent. These exceptions are that during the summer of 1918 the Land Banks at Wichita, St. Paul and Spokane were designated as financial agents of the government for the *sole* purpose of making seed grain loans to drought-stricken farmers. The President, at the request of the Secretary of Agriculture, set aside, out of his $100,000,000 of war funds, $5,000,000 for that purpose. These three banks made upwards of fifteen thousand seed loans, aggregating $4,500,000, all secured by crop liens. In making these loans, the three banks acted without compensation. This, under a joint circular of the Treasury and Agricultural Departments, which allowed actual expenses, but no more (Bill, Rec. 10).

(6) *Actual operations under the Act and government temporary aid authorized by and extended to Land Banks under the amendment of January 18, 1918.*

(a) Organized in 1916, the Board began active operations early in 1917. It is a matter of common knowledge that American investors looked upon the whole scheme as an invasion of the taxing power and control of the states, and as political, sectional, speculative, or as class legislation of a vicious nature. Anyhow, they would not buy the

farm loan bonds. In June, 1917, the Board, which to exist had to create a market, with the aid of a resourceful Secretary of the Treasury, made an agreement with a powerful New York banking syndicate to sell and the syndicate to buy, at par, fifty per cent of all the Land Bank bonds to be issued during the first six months, June 1 to November 30, 1917, with a provision that neither should, prior to 1918, sell any bonds to the public at less than 101½. The syndicate, in this indirect way, obtained from the public a commission of 1⅛ per cent for selling half of the six months' issue of bonds. This was but an expensive expedient to introduce the bonds on the market.

(b) The Land Banks were unable to sell any bonds directly to farmers having savings to invest, although this was the co-operative basis of the European acts. They were unable to sell them to ordinary investors, as predicted by the congressional advocates of the Act. They were unable to sell, even with the assistance of a great American banking syndicate, more than about one-half the amount provided for in the six months' syndicate contract. They were wholly unable to sell another bond after November, 1917, when that contract expired. A complete breakdown of the whole scheme was threatened. Thereupon, the constructive mind of the then Secretary of the Treasury again came to the front. The Act was, on January 18, 1918, amended so that he, upon request of the Board, could, out of any unappropriated public money, make *temporary* deposits, not in excess of $6,000,000, in and for the *temporary* use of the Land Banks. In plain words, money was at that time

on hand and had been or could be easily raised from the sale of Liberty bonds. This was the money which could, in this way, be loaned to Land Banks. Any such bank receiving the deposit was required to issue a demand certificate of deposit bearing a rate of interest not exceeding the current rate charged for other government deposits and to secure same by farm loan bonds or other collateral. The Secretary was permitted, during the fiscal years of 1918 and 1919, up to $100,000,000 per year, to likewise purchase farm loan bonds from Land Banks. Any such bank could, at any time, repurchase, on the same terms, the bonds so purchased, and, as to all such bonds as were held in the treasury, should upon demand do so, when one year elapsed after the end of the war. The original *temporary* organization of any Land Bank was required to be continued so long as any bonds so *temporarily* purchased should be held in the treasury and until the stock subscriptions made by the Farm Associations should equal the amount of stock held by the government (sec. 36, as amended January 18, 1918; 40 Stat. L. 431).

(c) Pursuant to the amendment, temporary deposits of large sums (Rec. 8) were made, for which two per cent certificates of deposit were issued. Of these there have been repaid (Rec. 8) large amounts. The Land Banks owned on September 30, 1919, $4,230,805 of United States bonds, and the Joint Stock Banks $3,287,503 thereof. The government temporarily took stock of the Land Banks aggregating $8,892,130, and on July 1, 1919, held $8,265,809 thereof. It purchased $149,775,000 of Land Bank bonds. Of these, it held on

July 1, 1919, $136,885,000. On September 30, 1919, the total issue of Land Bank bonds aggregated $285,600,000. Of these, $135,000,000 were held in the treasury under the amendment of January 18, 1918 (Bill, Rec. 9; Treasury Annual Reports, 1919, Finance, pp. 136-7).

(d) In addition to the Land Banks (*Supra*, par. [b]) twenty-seven of the Joint Stock Banks have been organized (Bill, Rec. 9; Appendix, Part 2, to the original Appellant's Brief, p. 91). Up to October 31, 1919, they had paid in $7,812,050 of capital, issued $46,225,000 of farm loan bonds, of which $41,000,000 are still outstanding (Bill, Rec. 11; Report No. 317, Senate Bill No. 3109, Calendar No. 270, 66th Congress, 2d Session; Treasury Annual Reports 1919, Finance, 1089). So un-American are these latter institutions, and so unfair to the public is the withdrawal of large investments from taxation, that the Senate Committee on Currency and Banking favorably reported (Report No. 317; Appendix, Part 2, to Appellant's Brief on former hearing, p. 91) a bill (*id.* Appendix, Part 3, *id.* p. 94) to repeal for the future all tax exemptions of the loan bonds upon the ground "that the tax exemption privilege ought never have been extended," and "the accumulation of large aggregations of capital, wholly exempt from any and all forms of taxation, is wrong in principle and should be discontinued." The committee was of opinion (*id.*) that, "the large taxpayers will gradually absorb these bonds, which will contribute nothing to the support of the government."

(e) Large private investors, *to escape taxation through the exemptions,* have taken large quantities of bonds. This is manifest from the fact that *private* investors hold about $150,000,000 (8 *supra,* subd. [6], par. [c] of the Land Bank and $41,000,000 (*id.* par. [d]) of the Joint Stock Bank bonds.

(f) The value of the tax exemption to the rich is apparent. The Magazine of Wall Street of July 10, 1920, gives an apt illustration. It lists the $26,050,430 holdings of the estate of Joseph R. DeLamar. The list shows "Federal Farm Loan 5's, $3,105,000, upon which fact it is in the article observed:

> "More than half of his municipal bonds consisted of Farm Loan 5's, as seen from Table II, evidently bought for their good yield combined with *tax exemption.*"

(g) Bond buyers are ever on the alert to make money at the expense of the government, so they artfully suggest a trade of Liberty bonds for Farm Loan bonds. This abuse, rendered possible by an illegal Act, is illustrated by a cunning suggestion to buyers (an example of many repeatedly made) on a card of a reputable investment company. It reads:

> "How to Make Your Liberty Bonds Earn Five Per Cent.
>
> Many people of modest means bought liberally of the first issue of Liberty Bonds.
>
> The succeeding issues earned a higher rate of interest so as to stimulate buying—but the citizen of modest means had bought his limit.

Today, those who have bought bonds and did not have an opportunity to exchange them to financial advantage, may secure a Government Bond bearing five per cent interest by exchanging Liberty Bonds of any issue at market price for Joint Land Bank bonds.

These bonds are instrumentalities of the United States Government, and are prepared and engraved by the Treasury Department. They are secured by Government approved first farm mortgages or by United States Government Bonds or Certificates of Indebtedness.

Joint Stock Land Bank bonds are exempt to the same degree as the Liberty Loan 3½'s —exempt from all taxes, except only inheritance taxes. This includes exemption from Federal Income Tax and local property taxes.

The value of exemption from Federal Income Taxes alone means added return, varying from 6½% to 18%—depending upon the amount invested.

These bonds are dated May 1st and November 1st of this year. They are redeemable at par and accrued interest on any interest date after five years from date of issue. Denominations $500 and $1,000.

We will be glad to explain the merit of the Land Bank issue without any obligation.

PEORIA COUNTY INVESTMENT CO.

508 Main St. Phone M. 6183 Peoria, Ill."

(h) The enormous value of the tax exemption was emphasized by the leading sellers of the Joint Stock Bank bonds, as shown by an advertisement in the New York Times of November 14, 1919. This appears as a frontispiece to the original brief

filed herein under the title "Brief for Appellant." It, among other things, recites:

> "TAX EXEMPTION: These bonds are exempt to the same degree as the Liberty Loan 3½'s—in other words, they are exempt from all taxes excepting only inheritance taxes. This includes exemption from Federal Income Tax and local personal property taxes.
>
> The value of the exemption from Federal Income Taxes alone, to individuals of large incomes, is indicated in the following figures, which would be further increased if the exemption of the bonds from other taxes were considered:

Net Yield of Joint Stock Bonds.

Taxable Incomes.	4½% (To Optional Date) Equivalent to	5% (From Optional Date to Maturity) Equivalent to
$ 50,000	6.52%	7.26%
80,000	8.33	9.25
100,000	10.22	11.36
200,000	12.60	13.89
500,000	15.52	17.24
1,000,000	16.07	17.86

> The top line represents the net rate realized from Joint Stock Land Bank Bonds, regardless of the income of the holder. The remaining figures represent the gross rate which must be realized at varying incomes from taxable securities to procure the net rate at the top of the column."

ASSIGNMENTS OF ERROR.

The assignments of error (Rec. 33) are that the court below erred in:

1. Decreeing a dismissal of the bill.

2. Holding to be valid and constitutional the Farm Loan Act, and also the amendment thereof, approved January 18, 1918.

3. Holding to be valid and constitutional each of the sections 21, 26 and 27 of the Farm Loan Act of July 17, 1916.

4. Holding that defendant can lawfully invest in and purchase Land Bank bonds.

5. Holding that the defendant can lawfully invest in and purchase Joint Stock Bank bonds.

QUESTIONS IN THE CASE.

I. These proceedings are such that the validity of the law can and should be tested therein (Argument, Div. I, pp. 28-29).

II. There not having been expressly or by fair implication surrendered by the Constitution to Congress the power to create Land and Joint Stock Banks, such power must be deemed not to have been in it, but reserved to the states or to the people (Argument, Div. II, pp. 29-42).

III. Appellees radically differ in their contentions. Part of them, the Joint Stock Banks, represented by Ex-Secretary McAdoo and Ex-Attorney General Wickersham, claim that the power to pass the Act had by the people been surrendered to the United States where, as here, the purpose was to create agencies to perform governmental functions. Others, the Land Banks through Ex-Justice Hughes, claim such power was surrendered, not in such way, but by the inherent right of a government to appropriate its public money for any public purpose (Argument, Div. III, pp. 43-46).

IV. The Act was, as matter of fact, never intended to provide agencies, the main purpose of which was to perform necessary and essential governmental functions, nor to provide for a federal appropriation of public money (Argument, Div. IV, pp. 47-64).

V. The Act cannot, as contended by Ex-Secretary McAdoo and Ex-Attorney General Wickersham, be sustained on the theory of the Joint Stock Banks, that it was an exercise of the power to establish agencies to perform necessary and essential governmental functions (Argument, Div. V, pp. 64-90).

VI. The passage of the Act cannot, as contended for by the Land Banks, through Ex-Justice Hughes, be sustained as an exercise of the power to appropriate the public money for public purposes (Argument, Div. VI, pp. 90-119).

VII. The exemption from taxation is unwarranted (Argument, Div. VII, pp. 119-126).

VIII. Even if the Act and its tax exemption feature can be upheld as to the Land Banks, they cannot be sustained as to the Joint Stock Banks (Argument Div. VIII, pp. 126-136).

ARGUMENT.

I.

These proceedings are such that the validity of the law can and should be tested therein.

The circumstances which gave rise to and surrounded these proceedings, already narrated in minute detail (Statement, Div. 2), remove any possible doubt as to the propriety thereof to test the grave constitutional questions argued. *Brushaber* v. *Union Pacific R. Co.*, 240 U. S. 1, 9, 10, is directly in point and a conclusive authority. There, in substance a similar proceeding, Mr. Chief Justice White significantly emphasized this thought:

> "* * * the defendant corporation having called the attention of the government to the pendency of the cause and the nature of the controversy and its unwillingness to voluntarily refuse to comply with the Act assailed, the United States, as *amicus curiae*, has at bar been heard both orally and by brief for the purpose of sustaining the decree."

These observations can here be applied with even greater force, for the questions involved have, by every interest, been fully argued, both orally and in print. The propriety of the proceedings has never been questioned by either the complaining stockholder or corporate defendant (the original parties to the cause), the intervening Land and Joint Stock Banks (the two classes of banks

covered by the Act), the United States, which appears herein *amicus curiae*, or the eminent and experienced counsel who broadly sought below and heretofore and now again seek here to have determined the validity of the legislation.

These remarks, while probably unnecessary, are prompted by a passing inquiry of Mr. Justice McReynolds at the former hearing.

II.

There not having been expressly or by fair implication surrendered by the Constitution to Congress the power to create Land and Joint Stock Banks, such power must be deemed not to have been in it, but reserved to the states or to the people.

(a) The Tenth Amendment to the Constitution provides:

> "Powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people."

To this simple provision effect has repeatedly been given and the rule is established that the power must be, by the Constitution, *expressly* granted or else be fairly implied from some other power which is actually expressed. In plain words, all powers were originally in the people. Such only as they, by the Constitution, *surrendered* to the United States exist in it. All others have been reserved to the states or to the people. This view is not in conflict, but fully accords, with

the general principle thus stated (*U. S.* v. *Harris*, 106 U. S. 629, 630, 636), by Mr. Justice Woods:

> "While conceding this, it must nevertheless be stated that the government of the United States is one of delegated, limited and enumerated powers. * * * Therefore, every valid Act of Congress must find in the Constitution some warrant for its passage. * * * Mr. Justice Story, in his Commentaries on the Constitution, says: 'Whenever, therefore, a question arises concerning the constitutionality of a particular power, the first question is whether the power be *expressed* in the Constitution. If it be, the question is decided. If it be *not* expressed, the next inquiry must be, whether it is properly an *incident* to an express power and necessary to its execution. If it be, then it may be exercised by Congress. If not, Congress cannot exercise it.' * * *"

Mr. Justice Nelson expressed exactly the same thought when (*Collector* v. *Day*, 11 Wall. 113, 124) he said:

> "The government of the United States therefore can *claim* no powers which are not granted to it by the Constitution, and the powers *actually* granted must be such as are *expressly* given or given by *necessary* implication."

This rule has been emphatically declared and enforced in the National Banking Cases (*M'Culloch* v. *Maryland*, 4 Wheat. 316; *Osborn* v. *Bank*, 9 Wheat. 738; *Bank* v. *Dearing*, 91 U. S. 29; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416), and applied to such subjects as the reclama-

tion of arid lands (*Kansas* v. *Colorado*, 206 U. S. 46) and child labor (*Hammer* v. *Dagenhart*, 247 U. S. 251) and to many others of *internal* concern, as shown by repeated decisions here rendered: (*Chisholm* v. *Georgia*, 2 Dallas 419, 435; *Martin* v. *Hunter's Lessee*, 1 Wheat. 304, 325; *Dobbins* v. *Erie Co. Comrs.*, 16 Pet. 435; *Ableman* v. *Booth*, 21 How. 506, 521; *License Tax Cases*, 5 Wall. 462, 470; *Collector* v. *Day*, 11 Wall. 113, 124; *Slaughter House Cases*, 16 Wall. 36, 62; *U. S.* v. *Cruikshank*, 92 U. S. 542, 549; *Claflin* v. *Houseman*, 93 U. S. 130, 136, 137; *Leisy* v. *Hardin*, 135 U. S. 100, 127).

Mr. Justice Story, in *Martin* v. *Hunter's Lessee*, 1 Wheat. 304, 325, said:

> "It is perfectly clear that the sovereign powers vested in the state governments, by their respective constitutions, remained unaltered and unimpaired, *except so far as they were granted to the government of the United States.*
>
> These deductions do not rest upon general reasoning, plain and obvious as they seem to be. They have been positively recognized by one of the articles in amendment of the constitution, which declares that 'the powers not delegated to the United States by the constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people.'
>
> The government, then, of the United States can *claim* no powers which are not granted to it by the constitution, and the powers actually granted must be such as are expressly given, or given by necessary implication."

Mr. Chief Justice Marshall, in *M'Culloch* v. *Maryland*, 4 Wheat. 316, 405, 410, said:

> "This government is acknowledged by all to be one of *enumerated* powers. The principle, that it can exercise only the powers granted to it, would seem too apparent to have required to be enforced by all those arguments which its enlightened friends, while it was depending before the people, found it necessary to urge. *That principle is now universally admitted.*
>
> * * * * * *
>
> In America, the powers of sovereignty are divided between the government of the Union and those of the states. They are each sovereign, with respect to the objects committed to it, and *neither sovereign with respect to the objects committed to the other.*"

Mr. Justice Iredell, in *Chisholm* v. *Georgia*, 2 Dallas 419, 435, 448, said:

> "Every state in the union in every instance where its sovereignty has not been delegated to the United States, I consider to be as completely sovereign, as the United States are in respect to the powers surrendered. The United States are sovereign as to all the powers of government *actually* surrendered. Each state in the Union is sovereign as to all the powers *reserved*. It must necessarily be so, because the United States have no claim to any authority but such as the states have *surrendered* to them. Of course, the part not *surrendered* must remain as it did before. * * * A state does not owe its origin to the government of the United States, in the highest or in any of its branches. It was in existence before it.

It derives its authority from the same pure and sacred source as itself. The voluntary and deliberate choice of the people."

Mr. Chief Justice Taney, in *Ableman* v. *Booth*, 21 How. 506, 516, said:

"The powers of the General Government, and of the state, although *both* exist and are exercised within the same territorial limits, are yet *separate* and *distinct* sovereignties, acting *separately* and *independently* of each other, within their respective spheres. And the sphere of action appropriated to the United States is as far beyond the reach of the judicial process issued by a state judge or a state court, *as if the line of division was traced by landmarks and monuments visible to the eye.*"

Mr. Justice Nelson, in *Collector* v. *Day*, 11 Wall. 113, 124, said:

"It is a familiar rule of construction of the Constitution of the Union, that the sovereign powers vested in the state governments by their respective constitutions, remained unaltered and unimpaired except so far as they were *granted* to the Government of the United States. That the intention of the framers of the Constitution in this respect might not be misunderstood, this rule of interpretation is expressly declared in the 10th article of the amendments, namely: 'The powers not delegated to the United States are reserved to the states, respectively, or to the people.' The Government of the United States, therefore, can *claim* no powers which are not granted to it by the Constitution, and the powers

> actually granted must be such as are *expressly given, or given by necessary implication.*
>
> The General Government, and the States, although both exist within the same territorial limits, are separate and distinct sovereignties, acting separately and independently of each other, within their respective spheres. The former, in its appropriate sphere, is supreme; but the *States within the limits of their powers not granted, or, in the language of the 10th Amendment, 'reserved,' are as independent of the General Government as that government within its sphere is independent of the States.*"

Dobbins v. *Erie County Commissioners*, 16 Pet. 435, 447, asserts the same principle, while in *Van Brocklin* v. *Tennessee*, 117 U. S. 151, 178, the last of the foregoing italicized words of Mr. Justice Nelson were by Mr. Justice Gray quoted with approval.

Mr. Chief Justice Waite, in *United States* v. *Cruikshank*, 92 U. S. 542, 549, said:

> "We have in our political system a Government of the United States and a government of each of the several states. Each one of these governments is distinct from the others, and each has citizens of its own who owe it allegiance, and whose rights, within its jurisdiction, it must protect. The same person may be at the same time a citizen of the United States and a citizen of a State, but his rights of citizenship under one of these governments will be different from those he has under the other. *Slaughter-House Cases*, 16 Wall. 74.
>
> Citizens are the members of the political community to which they belong. They are

the people who compose the community, and who, in their associated capacity, have established or submitted themselves to the dominion of a government for the promotion of their general welfare and the protection of their individual as well as their collective rights. In the formation of a government, the people may confer upon it such powers as they choose. The government, when so formed, may, and when called upon should, exercise all the powers it has for the protection of the rights of its citizens and the people within its jurisdiction; but it can exercise no other. *The duty of a government to afford protection is limited always by the power it possesses for that purpose.* * * * Within the scope of its powers, as *enumerated* and *defined*, it is supreme and above the States; but *beyond, it has no existence.* It was erected for *special* purposes, and endowed with all the powers necessary for its own preservation and the accomplishment of the ends its people had in view. *It can neither grant nor secure to its citizens any right or privilege not expressly or by implication placed under its jurisdiction.*

The people of the United States resident within any State are subject to two governments: one State and the other National; *but there need be no conflict between the two. The powers which one possesses, the other does not.* They are established for different purposes, and have separate jurisdictions. Together they make one whole, and furnish the people of the United States with a complete government, ample for the protection of all their rights at home and abroad."

Mr. Justice Bradley, in *Claflin* v. *Houseman,* 93 U. S. 130, 136, said.

> "Every citizen of a State is a subject of two distinct sovereignties, having concurrent jurisdiction in the State; concurrent as to place and persons, though distinct as to subject matter * * *.
>
> It is true, the sovereignties are distinct, and *neither can interfere with the proper jurisdiction of the other,* as was so clearly shown by Chief Justice Taney in the case of *Ableman* v. *Booth,* 21 How. 506."

Mr. Chief Justice Chase, of the internal commerce and the domestic trade of a state, *License Tax Cases,* 5 Wall. 462, 470, said:

> "Over this commerce and trade Congress has no power of regulation, nor any direct control. This power belongs exclusively to the States. No interference by Congress with the business of citizens transacted within a State is warranted by the Constitution, except such as is *strictly* incidental to the exercise of powers *clearly* granted to the Legislature. *The power to authorize a business within a State is plainly repugnant to the exclusive power of the State over the same subject."*

In making application of the principle to the police power, Mr. Justice Miller (*Slaughter-House Cases,* 16 Wall. 36, 62) said:

> "This is called the police power; and it is declared by Chief Justice Shaw that it is much easier to perceive and realize the existence and sources of it than to mark its boundaries,

or prescribe limits to its exercise. *Com.* v. *Alger,* 7 Cush. 84. * * *

This power is, and must be from its very nature, incapable of any very exact definition or limitation. Upon it depends the security of social order, the life and health of the citizen, the comfort of an existence in a thickly populated community, the enjoyment of private and social life, and the beneficial use of property. * * *

In *Gibbons* v. *Ogden,* 9 Wheat. 203, Chief Justice Marshall, speaking of inspection laws passed by the States, says: 'They form a portion of that immense mass of legislation which controls everything within the territory of a State not surrendered to the General Government—*all which can be most advantageously administered by the States themselves.* Inspection laws, quarantine laws, health laws of every description, as well as laws for regulating the *internal* commerce of the State, and those which respect turnpike roads, ferries, etc., are component parts. *No direct general power over these objects is granted to Congress; and consequently they remain subject to state legislation.*

The exclusive authority of state legislation over this subject is strikingly illustrated in the case of *New York* v. *Miln,* 11 Pet. 102. * * *

To the same purpose are the recent cases of *The License Tax,* 5 Wall. 471, and *United States* v. *Dewitt,* 9 Wall. 41."

So Mr. Justice Gray (*Leisy* v. *Hardin,* 135 U. S. 100, 127) of the same subject, said:

"By the Tenth Amendment, 'the powers not delegated to the United States by the Consti-

> tution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.'
>
> Among the powers thus reserved to the several States is what is commonly called the police power—*that inherent and necessary power, essential to the very existence of civil society, and the safeguard of the inhabitants of the State against disorder, disease, poverty and crime.*"

In Cooley's Constitutional Limitations (7th Ed.) 831, it is upon the same subject said:

> "In the American constitutional system, the power to establish the ordinary regulations of police has been left to individual states, and it cannot be taken from them, either wholly or in part, and exercised under legislation of Congress. *Neither can the national government, through any of its departments or officers, assume any supervision of the police regulations of the States. U. S.* v. *Dewitt,* 9 Wall 41; *U. S.* v. *Reese,* 92 U. S. 214; *U. S.* v. *Cruikshank,* 92 U. S. 542; *Keller* v. *U. S.,* 213 U. S. 138."

From the principles thus established the language of Judge Cooley may be paraphrased by the conclusion that "in the American constitutional system the power to establish" *private* corporate agencies to do a *private* loan business "has been left to individual states, and it cannot be taken from them, either wholly or in part, and exercised under legislation of Congress."

(b) As the states are, by the Act, for an ***unlimited*** time deprived of their control of and their

taxing power over a valuable form and an *unlimited* amount of private investment (*Farmers & Mechanics Bank* v. *Minnesota,* 232 U. S. 516, 521), the question whether the power to pass such a law rested in the states or in the United States should be approached in the light of the foregoing principles recently and thus by Mr. Justice Day (*Hammer* v. *Dagenhart,* 247 U. S. 251, 255) accurately restated:

> "In interpreting the Constitution it must never be forgotten that the nation is made up of states, to which are intrusted the powers of local government. And to them and to the people the powers not expressly delegated to the national government are reserved. (*Lane County* v. *Oregon,* 7 Wall. 71, 76.) The power of the states to regulate their purely *internal* affairs by such laws as seem wise to the local authority is *inherent,* and has never been surrendered to the general government. *New York* v. *Miln,* 11 Pet. 102, 139; *Slaughter House Cases,* 16 Wall. 36, 63, 64; *Kidd* v. *Pearson, supra.*"

That the power to establish the agencies, like the Land and Joint Stock Banks, was *internal* and rested *exclusively* in the states is conclusively settled by *Kansas* v. *Colorado,* 206 U. S. 46, 87, 88, 90, 91. There it was decided that there could not, from the general welfare clause, or any *other* provision of the Constitution, be found or implied any power in Congress to reclaim arid land. No mere extract could do full justice to the opinion of Mr. Justice Brewer in that case. After declaring that

the United States was a government of enumerated powers, he, among other things, said:

> "As heretofore stated, the constant declaration of this court from the beginning is that this government is one of enumerated powers. * * * Turning to the enumeration of the powers granted to Congress by the 8th section of the 1st article of the Constitution, it is enough to say that no one of them, by any implication, refers to the reclamation of arid lands. * * * But the proposition that there are legislative powers affecting the nation as a whole which belong to, although not expressed in, the grant of powers, is in direct conflict with the doctrine that this is a government of enumerated powers. That this is such a government clearly appears from the Constitution, independently of the Amendments, for otherwise there would be an instrument granting certain specified things made operative to grant other and distinct things. This natural construction of the original body of the Constitution is made absolutely certain by the 10th amendment. This Amendment, which was seemingly adopted with prescience of just such contention as the present, *disclosed the widespread fear that the national government might, under the pressure of a supposed general welfare, attempt to exercise powers which had not been granted.* With equal determination the framers intended that no such assumption should ever find justification in the organic act, and that if, in the future, further powers seemed necessary they should be granted by the people in the manner they had provided for amending that act. * * * The argument of counsel ignores the principal factor in this

article, to-wit, 'the people.' Its principal purpose was not the distribution of power between the United States and the states, but a reservation to the people of all powers not granted. The preamble of the Constitution declares who framed it, 'we the people of the United States,' not the people of one state, but the people of all the states; and article 10 reserves to the people of all the states the powers not delegated to the United States. The powers affecting the internal affairs of the states not granted to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, and all powers of a national character which are not delegated to the national government by the Constitution are reserved to the people of the United States. The people who adopted the Constitution knew that in the nature of things they could not foresee all the questions which might arise in the future, all the circumstances which might call for the exercise of further national powers than those granted to the United States, and, after making provision for an amendment to the Constitution by which any needed additional powers would be granted, they reserved to themselves all powers not so delegated. This article 10 is not to be shorn of its meaning by any narrow or technical construction, but is to be considered fairly and liberally, so as to give effect to its scope and meaning. * * * This very matter of the reclamation of arid lands illustrates this: At the time of the adoption of the Constitution, within the known and conceded limits of the United States there were no large tracts of arid land, and nothing which called for any further action than that which might be taken by the

> legislature of the state, in which any particular tract of such land was to be found; and the Constitution, therefore, makes no provision for a national control of the arid regions or their reclamation. But, as our national territory has been enlarged, we have within our borders extensive tracts of arid lands which ought to be reclaimed, and it may well be that no power is adequate for their reclamation other than that of the national government. But if no such power has been granted, none can be exercised."

If, as will be hereafter demonstrated (*Infra*, Div. V), the ***main*** functions to be exercised by the corporations authorized to be created, were ***private*** and not ***governmental***, then, as Mr. Chief Justice Marshall (*Osborn* v. *Bank*, 9 Wheat. 738, 860), expressly stated, "it has never been supposed that *Congress* could create such a corporation." It would seem, therefore, that the principle established by these two decisions nullifies the force of the Act, and makes applicable the terse statement of Mr. Justice Day in the Child Labor case (*Hammer* v. *Dagenhart*, 247 U. S. 251, 255), that to sustain this statute "would sanction an invasion by the federal power of the control of a matter purely local in its character, and over which no authority has been delegated to Congress * * *." This certainly is true unless there was, by some ***enumeration*** in the Constitution, ***surrendered*** to the United States, the clear power to establish the Farm Loan System.

III.

Appellees radically differ in their contentions. Part of them, the Joint Stock Banks, represented by Ex-Secretary McAdoo and Ex-Attorney General Wickersham, claim that the power to pass the Act had by the people been surrendered to the United States where, as here, the purpose was to create agencies to perform governmental functions. Others, the Land Banks, through Ex-Justice Hughes, claim such power was surrendered, not in such way, but by the inherent right of a government to appropriate its public money for any public purpose.

Counsel for the appellees do not agree as to how or in what manner there was surrendered to Congress power to pass the Act. Their differences are radical.

(a) Ex-Secretary McAdoo and Ex-Attorney General Wickersham, in elaborate printed arguments, voice the view that the *power* to pass the Act is found in the doctrine of the National Bank Cases (*M'Culloch* v. *Maryland*, 4 Wheat. 416; *Osborn* v. *Bank*, 9 Wheat, 738; *Bank* v. *Dearing*, 91 U. S. 29; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416), that the express duty of establishing and maintaining a government *implies* the power to establish, as part thereof, those agencies which perform *necessary* and *essential* governmental functions. Upon this theory *alone* Congress passed the Act (53 Cong. Rec. 453, 489, 64 Cong. 1 Session, Senate Report No. 144; House Doc. No. 494, 53 Cong. Rec. 7246). However, it

deemed it unimportant (53 Cong. Rec. 7246) that the governmental functions were slight and insignificant, and at most mere *possibilities* (Infra. Div. V, subd. 6th), provisions for which were inserted as a device and makeshift to make that constitutional which otherwise would be unconstitutional. This theory of these banks was, in 1918 and 1919, outlined by *widely* circulated printed opinions of these lawyers and several *other* leaders of the profession. Upon these opinions the Joint Stock Bank bonds were by bond-sellers offered, and upwards of $41,000,000 sold to investors. These opinions appear in a government printed document of November 13, 1919, entitled:

> "Amendment to Federal Farm Loan Act. Hearings before the Committee of Banking and Currency of the House of Representatives in H. R. 8159, a bill to amend the Act of Congress, approved July 17, 1916, known as the Federal Farm Loan Act to increase the limit of loans."

It is of significance that they all bear date more than a year *after* the opinion of Ex-Justice Hughes to the Land Banks, to which reference is about to be made, and which attempted to rest the validity of the Act on an entirely different *ground*, i. e., on the power to appropriate public money. Of course, power to issue Joint Stock Bank bonds could not be found in the right of Congress to appropriate public money, for no money was to be or was ever appropriated for such banks. Hence to sustain the Act as to them,

the right to pass it must be found in some power other than that of appropriation.

(b) Ex-Justice Hughes was by the Land (not the Joint Stock) Banks on May 4, 1917, *after the passage of the Act*, called upon for an opinion on the validity of the Land Bank bonds, and gave one to them that *their* bonds were valid on the *sole* ground that the Act was an exercise of the power to appropriate public money for the good of the public. This view does not appear from any published document to have been ever *before* advanced by any judge, lawyer or statesman. It is, however, herein, by him, sought to be here maintained in an elaborate printed argument, written *after* and in the light of the printed opinions of Ex-Secretary McAdoo and Ex-Attorney General Wickersham and the other lawyers who concurred with them. It must then be assumed that he rejects their views.

This opinion of Ex-Justice Hughes was printed, published by the Thomsen-Bryan-Ellis Co., of Baltimore, Washington, New York and Philadelphia, and given wide circulation. The title of the pamphlet in which it appeared, was:

> "Federal Land Bank Bonds. Opinion of Former Supreme Court Justice Charles E. Hughes, confirming validity of the above bonds and their exemption from taxation."

In passing it may be repeated that if this view is sound, then, at least, so much of the Act as authorizes the establishment of the Joint Stock Banks is void because there was, as to them, no appropriation.

(c) These *opposing* views of counsel rest upon entirely *different* grounds and must, therefore, be given *separate* consideration. The claim of the Joint Stock Banks as presented by Ex-Secretary McAdoo, Ex-Attorney General Wickersham and the lawyers who joined with them, is considered in Division IV of this brief; that of Ex-Justice Hughes in Division VI.

It may, however, be remarked the House and Senate did not wholly agree as to where the power rested. Thus the joint House and Senate committee (53 Cong. Rec. 453, 489, 64 Cong. 1st Session, Senate Report No. 144; House Document No. 494) reported that *loaning* of *private* money to farmers was conceived "to be a *proper* function of the government." But on the floor of the Senate it was in debate (53 Cong. Rec. 7246) by Senator Cummins said:

> "It is necessary, however, to *find* some governmental purpose, *however slight or insignificant,* in order to invoke the authority of Congress in the incorporation and *therefore* it is declared that these Land Banks *shall* be public depositaries."

The great senator was wrong in saying that it was provided that these banks "*shall* be public depositaries." All the Act says is that they *may* be so designated. There is some difference in a mandatory requirement and a remote possibility (*Infra*, Div. V, subd. 6th).

IV.

The Act was, as a matter of fact, never intended either to provide agencies, the main purpose of which was to perform necessary and essential governmental functions, nor to provide for a federal appropriation of public money.

That the Act was, *as a matter of fact*, never so intended is perfectly plain, for these reasons:

(1st) *The purpose was not to provide agencies which were in the main to perform essential and necessary governmental functions.*

(a) The House and Senate joint committee reported (53 Cong. Rec. 453, 489; 64th Cong. 1st Session, Senate Report 144; House Document No. 494, Report No. 630) that the *sole* purpose of the Act was the loaning of money to farmers—declaring that "such we conceive to be a proper function of the government." In the Senate debate, Senator Cummins said (53 Cong. Rec. 7246) that to make the Act constitutional it was deemed necessary to add some provision "however small or insignificant" for the agencies created to perform some governmental function. This was done by section 6 hereafter (*Infra*, Div. V, subd. 6th) discussed. There can then be no doubt of the *real* purpose of the Act.

(b) If anything more is needed to be said as to this matter it may be remarked that it is at least plain that the purpose of the Act was not to provide agencies, the *main* functions of which were to assist the government in performing its *necessary* and *essential* duties. So it was by Charles A. Enslow (10 Lawyer and Banker, and Southern

Bench and Bar Review, October, 1917, p. 402) aptly said:

> "The Federal Farm Loan Bank is nothing more nor less than a corporation chartered by the national government, and whose *sole* object is to secure from a certain class of people of the United States, money to be loaned to another class of people at a reduced interest rate. *It never was intended to be anything other than that.*"

The *real* and only purpose was to enable owners of farm land, not necessarily farmers, to borrow, for any purpose, money on farm mortgages for very long terms (in some instances up to fifty years) at extremely low rates of interest. This is clearly shown by its language as well as by the congressional debates (53 Cong. Rec. 6793, 6795, 6796, 6861, 6961, 6965, 6968, 7026, 7129, 7245, 7246, 7305, 7317) and by the governmental literature and official announcements (*Infra* subd. 2d). As correctly declared by Senator Cummins in debate (53 Cong. Rec. 7246), "the *chief* purpose is to secure a lower rate of interest to those who borrow; that is its *only* object."

The whole subject could here rest. If there is any disposition to further follow it, it may be stated that the history of the movement to establish in the United States a system of rural credits, based on the German plan of collective and co-operative borrowing and lending of money on long time farm mortgages, appears in Agricultural Co-operation and Rural Credit in Europe (1913) 63 Cong. 1st Session, Senate Doc. Nos. 17 and 214,

Parts I, II and III; id., 2d Session, Report of the American Commission (1914), Senate Doc. No. 261, Parts I, II; id., Report of the U. S. Commission on Agricultural Credit (1914) Senate Doc. No. 380; 64th Cong. 1st Session, Report of Joint Committee on Rural Credits (1916) House Doc. No. 494; id., Report of Committee on Banking and Currency (1916) House Report No. 630; id., Conference Report (1916) Senate Doc. 472; see also Rural Credits (1915) 64th Cong., 1st Session, Senate Doc. No. 9; 63d Cong. 1st Session (1913) Senate Doc. No. 114; Hearings before the Subcommittee of the Committee on Banking and Currency (H. R.) on Rural Credits (1913), and Joint Hearings before the Subcommittees of the Senate and House Committees on Banking and Currency on Rural Credits (1914).

The debates and committee reports may be resorted to, not to vary, limit or broaden the construction of the language, but to advise the court of the *intention* of Congress in order that such intention shall indicate the scope and purpose of the Act and the subject sought to be dealt with (*U. S.* v. *St. Paul M. & M. Ry. Co.*, 247 U. S. 310, 318, and cases cited; *McLean* v. *U. S.*, 226 U. S. 374, 380; *Standard Oil Co.* v. *U. S.*, 221 U. S. 1, 50).

(c) That the scheme was, in fact, *private* in its nature and not *governmental* is also apparent from every provision of the Act. It has, from the very first, been so recognized. Governor Herrick, *previous* to its passage, had given much thought to a Farm Loan System, writing such leading arti-

cles as How to Finance the Farmer (64 Cong. 1st Session, Sen. Doc. 396), How to Finance the Farmer—Private Enterprise—Not State Aid (1915, State Committee on Rural Credits and Co-operation, 920 Cuyahoga Building, Cleveland, Ohio), and Rural Credits, Lands and Co-operation (pamphlet). Immediately after the passage of the Act, he reviewed and condemned it (119 Atlantic Monthly, 222, 225, February, 1917) in a masterly article. In speaking of the demands of union labor for a like congressional scheme to aid in building homes for its members, he observed:

> "However, the government must address itself to meeting these demands and difficulties, or else get out of the *private* business of lending money for agricultural purposes."

In the same article he quotes Ex-Secretary McAdoo as saying that the government will not

> "stand for a proposition to lend money to *private* corporations or individuals upon the security of mortgage."

He also said (id. p. 223) this:

> "Congressman Caraway of Arkansas was *one of the ardent advocates,* but in a speech in November before the Farm Mortgage Bankers' Association, he said: 'I do not believe in the government's going into *private* business of any kind, but this is one of the things it is going to do.'"

(d) In the case of the Joint Stock Banks, there is not even the flimsy pretense (which is claimed to exist in the case of the Land Banks) that the power of appropriation was exercised or that the money raised by the mortgages was to be used for agricultural development. There was for them no appropriation and there is *no limit or restriction whatever* as to the *purposes* for which the money loaned may be used, as those banks are expressly exempted from the limitations imposed upon Land Banks in that respect. Even the co-operative and collective plan of borrowing by the farmers, the joint and several liability of the banks, and the degree of federal supervision, which exist in the case of the Land Banks, were the strongest arguments advanced in Congress in favor of the Act. These were specifically *dispensed with* in the case of the Joint Stock Banks, because it was thought that some farmers might object to a co-operative undertaking with their neighbors, or to the publicity and scrutiny thereby entailed (Senate Rep. 144, p. 11; House Rep. 630, p. 910; 1st Annual Rep. of Federal Farm Loan Board, p. 22).

These banks are expressly prohibited from receiving deposits or doing any banking or other business (sec. 16). In Congress it was (64 Cong. 1st Sess. Senate Rep. 144, p. 11; House Doc. 494, p. 14, Report 630, p. 10) reported:

> "Joint Stock Land Banks are not permitted to engage in *any* business but making farm mortgage loans and issuing bonds."

In the Farm Loan Primer, p. 15; Ed. July 23, 1918, it is stated:

> "These Joint Stock Land Banks are *private institutions* intended for the investment of *private capital.*"

The bill (Rec. 5) alleged, and the motion to dismiss (Rec. 11) conceded, that *private* persons as shareholders own and operate the Joint Stock Banks purely and *exclusively* for their own individual and *private* profit.

(e) But the functions of Land Banks are also purely *private*. The farm mortgages executed *to* both classes of banks and the bonds issued *by* them thereon, and held by *private* investors are wholly instruments of *private* business. They, like the Joint Stock Banks (section 16), can do no *banking* (section 14), and do not possess any of the characteristics of these institutions which have ever been held to be instrumentalities of the government. The bonds of both classes of banks are neither assets nor liabilities of the United States. It does not promise to pay or guarantee the payment of them. The money raised thereon does not go to it.

(2d) *Not only were the agencies intended to be strictly private, but there was a distinct purpose not to appropriate public money or lend it on the credit of the government.*

(a) The quotations, from the congressional debates and committee reports and the government official announcements, hereinafter set forth, all show that there was actually, no *real*

purpose to provide *necessary* and *essential* governmental agencies, nor to appropriate money nor lend any public credit. They do, however, affirmatively show, as Senator Cummins (53 Cong. Rec. 7246) stated, and the House Committee (64 Congress, 1st Session, Report No. 630) reported, that the *sole* and *only* object sought to be attained was to give the farmers long-time loans on farm mortgages at *low* interest rates.

In introducing the bill, the Joint Committee made this (53 Cong. Rec., 453, 489, 64th Cong., 1 Sess., Senate Report No. 144 and House Doc. No. 494) report:

> "* * * This bill *enables the farmer to obtain capital* for productive purposes, at *low* rates and for long terms, on the security of his farm. * * * The American farmer does not come to congress with a hard-luck story. *He does not ask the government to bestow on him the public money that all the people have contributed in taxes.* He does not demand that the government become a banker in order to borrow money on bonds and loan the proceeds to him. He merely calls attention to the fact that farming has become a business demanding large amounts of capital; he points out the undoubted excellence of the security he offers; and he demands legislation that shall put it in the power of *those who are interested,* and those who have money to invest, to extend to him the credit he requires. He desires the government to authorize a system of land banks which shall duplicate for him the facilities now com-

manded by men engaged in manufacturing, in transportation, and in commerce. * * *

Of money seeking long-term investment at low rates there is an abundant supply. It includes the ordinary savings of the school teacher, clerk, minister and wage earner; the proceeds of life insurance in the hands of widows and other beneficiaries; funds belonging to estates, minors, and wards in chancery in the hands of executors, guardians, and trustees; funds of insurance companies, benevolent orders, and societies of various kinds; endowment of colleges, hospitals, museums, and other institutions; and assets to be invested by receivers, courts, and governments. The aggregate of these is enormous. They require an investment that is absolutely safe and reasonably liquid in the sense that it may be converted into cash upon moderate notice; in other words, that it may find a ready market. A safe investment of this character need not carry a high rate of interest. *Here we discover the funds that should be made available to the farmer on long-term mortgage.*

We may picture the owners of this vast wealth grouped on one side of a river, the farmers desiring loans grouped on the other side. It is evident that each has what the other wants. We are asked to furnish the bridge which shall bring them in touch, or rather to *grant a franchise to those who will build the bridge* if we will construct the approaches. *Such we conceive to be a proper function of the government.* * * *

It is believed that the system of land banks outlined in the proposed bill affords a safe and attractive farm loan bond for the *investing public; low interest rates,* long

term mortgages, and *easy payments* for the farmers; low cost of administration; simplicity of organization and operation; adaptability to the needs of every section; and stimulation to the spirit of generous cooperation among farmers."

The House Committee on Banking and Currency (64th Cong. 1 Sess., Report No. 630, p. 2) reported:

"The immediate purpose of this bill is to afford those who are engaged in farming or who desire to engage in that occupation a vastly greater volume of land credit *on more favorable terms* and at *materially lower* and more nearly uniform *interest rates* than at present available. The means whereby this purpose is to be accomplished is provided through the establishment of national chartered and government supervised organizations to grant long-time, amortizable loans at *low interest rates* upon farm mortgage security; to assemble in each organization individual farm mortgages into one collective security; and to issue upon this collective security credit instruments to be known as farm loan bonds of such safety and soundness as to command the investment funds of the country in abundance. * * * In stating that the *immediate purpose* of the bill is to secure greater credit accommodation for the farmer, the committee has had in mind the capital requirements of the farmer. Although the fact has been until recently almost entirely ignored, it is true that agriculture is a business as much as manufacturing or commerce is a business. With the rapid increase in population and

> the accompanying rapid rise in land value it has become more and more necessary that successful farming shall be conducted as a business. Modern agriculture needs and demands capital in constantly increasing volume. * * * A new form of credit instrument is created—the farm loan bond. This bond is issued upon the capital of the land bank and the collective security of first mortgages. Every precaution has been taken to make it an absolutely safe form of investment. These bonds are sold to investors and the funds obtained are loaned to the farmer borrowers. * * * It is from the sale of Farm Loan Bonds that the Land Banks will be enabled to secure the funds to loan to the farmer."

In the course of the debate, Senator Robinson on May 2, 1916 (53 Cong. Rec. 7228), said:

> "The *primary purpose of* this legislation is to secure long time loans at *low rates of interest* to those who, under the terms of the act, may avail themselves of its provisions."

Senator Cummins (id., p. 7246) said:

> "The *chief purpose* of the corporation as avowed by all who have spoken in its behalf, and, as I think, will be admitted by everybody, is to secure a *lower rate of interest* to those who borrow from the Land Banks; *that is its only object.*"

Senator Hollis, who had charge of the bill (id., p. 6793), said:

> "If I did not believe that the bill would give the farmer a *lower rate* than he is

now getting, I should not think it would be worth while to pass the bill. It is because we feel the farmer is not now getting loans at as *low a rate* as he is entitled to that we are passing the bill. If it has that result, I shall feel that we have *achieved our object.*"

The government's official announcements of the purpose and scope of the Act are equally plain. Thus the Act (sec. 3) requires to be issued from time to time *official* publications "setting forth the principal features of this Act and * * * the merits and advantages of farm loan bonds."

Accordingly the treasury department has issued a number of circulars and reports from which these extracts are taken:

Circular No. 1 (March 20, 1917):

"These associations are organized for the primary *purpose* of giving to each borrower the benefit of the combined credit of all its members to the extent of the capital contributed and the limited liability they each incur, and hence the associations are required to endorse every loan made to members."

Circular No. 2 (March 20, 1917):

"What the Farm Loan Act promises:

"*Farmers want cheaper money.* They ought to have it. The Federal Farm Loan Act aids them to get it. * * * The Federal Farm Loan Act *provides a way* of getting mortgage loans for farmers at *low rates* of in-

terest, at lengths of time to suit the borrower and on *easy terms* of repayment. * * *"

Circular No. 3 (February 9, 1917):

"The law is a great new agency for furnishing money to *finance the business of farming.*"

The Farm Loan Primer (p. 3):

"Q. What are the *general purposes* of the Federal Farm Act?

Ans. To *lower* and equalize interest rates on first mortgage farm loans; to provide long term loans with the privilege of repayment in installments through a long or short period of years at the borrower's option; to assemble the farm credits of the nation, to be used as security for money to be employed in farm development; to stimulate cooperative action among farmers; *to check land monopoly by making it easier for tenants to get land;* and to provide safe and sound long term investments for the thrifty."

The First Annual Report of the Federal Farm Loan Board (pp. 13, 17, 22) recites:

"* * * The Federal Farm Loan Act was enacted to create an institution which would furnish farmers with money at a *reasonable rate* and not be run on a profit producing basis. * * * In order to provide capital for agricultural development at the *lowest possible rate of interest,* which was, of course, the primary purpose of the Act, it was essential. * * * The *general purpose* of the act was to provide for the farm loan needs of the country."

(b) The entire scheme if justified, either as providing *necessary* governmental agencies, or as an appropriation, would be contrary to the view of the American Commission (63rd Cong. 2d Sess., Sen. Doc. 261, Part 1, p. 13), which reported:

> "It is the opinion of the commission that our American problem of rural credit should be worked out *without government aid*. If there is not *private* capital in sufficient quantities, the only way the government can get the needed capital is either by *taxing all the people* in order to get capital for farming, or else by issuing bonds that sometime later must be *paid by all* the people. * * * One of the great lessons learned in Europe is that in the long run the farmers succeed best when they help themselves. Whenever they become dependent on the government they keep looking to the government for more aid. It is believed to be a correct general statement that rural credit is on the strongest basis in those countries, where it has been developed most completely *without government aid*. Even granting the great importance of agriculture, *it is improper for all the people to be taxed in order to assist the prosperity of even a great class like the farming class*. Anything in the way of national favors or opportunities for borrowing money on land would be almost certain to encourage speculation in land. This would lead to still higher prices for land and still greater difficulty in getting the land into the hands of owners who till it. It is sometimes urged that the government should loan money directly to farmers at a very low rate of interest. * * * It is doubtful if it will

help the farmers in the long run if they are given special privileges. In other words, the government should help bring about a better system of rural credit by legislation, *but not by subsidy.*"

The United States Commission in its report to Congress (63d Cong. 2d Sess., Sen. Doc. 380, p. 22) said:

> "*It is our opinion that such aid should not be extended in the United States.* * * * The idea of federal aid is always attractive and commands many able, earnest advocates: *but self help should be the motto of our new agriculture.* If given the opportunity, under liberal enactment of law, the savings of our nation will gladly invest in this safe field *and relieve the federal treasury of any necessity to finance the project.* It is wise legislation, *rather than liberal appropriations* or loans, which rural credit mostly needs at our hands."

President Wilson, entertaining the same view, in his first annual message of December 2, 1913, (119 Atlantic Monthly, February, 1917, p. 222) said:

> "The farmers, of course, ask and should be given *no special privilege, such as extending to them the credit of the government itself.* What they need and should obtain is legislation which will make their own *abundant and substantial credit resources* available as a foundation for joint, concerted local action in their own behalf in getting capital they must use. It is to this we should now address ourselves."

The then Secretary of the Treasury McAdoo, in a ship subsidy speech before the Chamber of Commerce at Washington, on February 4, 1915, (119 Atlantic Monthly, February, 1917, p. 222) said:

> "Yet, gentlemen, when we cannot get a state of the American Union to pay its just debts to the government for money loaned to it, you ask us to stand for a proposition to lend money to private corporations or individuals upon the security of mortgage. Never on the face of the earth! And I tell you, gentlemen, if you ever enter upon it, you will have to lend it upon railroads and upon every other enterprise. Bills are referred to me asking that every conceivable sort of scheme be approved, submitting them for the judgment of the department, for raids upon the United States Treasury in the form of actual loans to be made by the treasury of the United States on this thing and that thing—farm loans, loans on houses built by workingmen, and so on. They are all entitled to consideration if we are going into the money-lending business. We shall have to lend it to everybody. You cannot discriminate under our system of government. Everybody must tap the treasury till, if you adopt any such resolution as this."

The then Secretary of Agriculture Mr. Houston, (119 Atlantic Monthly, February, 1917, p. 222) in his annual report of 1914, said:

> "The chief difference of opinion arises over whether there should be special aid furnished (to farmers) by the government. *There seems to be no emergency which re-*

quires or justifies government assistance to the farmers directly through the use of the government's cash or the government's credit. The American farmer is sturdy, independent, and self-reliant. He is not in the condition of serfdom or semi-serfdom in which were some of the European peoples to whom government aid was extended in some form or other during the last century. He is not in the condition of many of the Irish peasantry for whom encouragement and aid have been furnished through the land-purchase act. As a matter of fact, the American farmers are more prosperous than any other farming class in the world. As a class they are certainly as prosperous as any other great section of the people; as prosperous as the merchants, the teachers, the clerks, or mechanics. It is necessary only that the government provide machinery for the benefit of the agricultural classes as satisfactory as that provided for any other class. It is the judgment of the best students of economic conditions here that there is needed to supplant existing agencies a proper land-mortgage banking system operating through private funds, just as other banking institutions operate, and this judgment is shared by the leaders of economic thought abroad."

At the expense of repetition there may here be emphasized the thought, that the Senate Committee on Banking and Currency and the Joint House and Senate Committee on Rural Credits in 1916 (64th Cong. 1st Sess., House Doc. 494, p. 6) reported:

"The American farmer does not come to Congress with a hard luck story. *He does*

> *not ask the government to bestow on him the public money that all the people have contributed for taxes.* He does not demand that the government become a banker in order to borrow money on bonds and loan the proceeds to him. * * * He demands legislation that shall put it in the power of those who are interested and *those who have money to invest to extend to him the credit he requires.*"

Upon these recommendations the Farm Loan Act was passed. The statements were so emphatic that a deep student of the subject (119 Atlantic Monthly, 222, 223, February, 1917) was led to say:

> "All this is sound doctrine, and since it was thus *deliberately* pronounced as a rule of action for the administration by the *foremost* three of its leaders, nobody, of course, could have predicted the Federal Farm Loan Act. That such a law should really exist still seems incredible, not only because it violates every principle of this doctrine, but because it is unjustified by any emergency * * *."

(c) It would therefore seem impossible to conceive that Congress, in fact, ever *intended* to exercise either of the two *alleged* powers about the existence of which counsel so radically differ. The most of that intent seems to have been that the Joint Committee (64 Cong. 1 Sess., Report 630, p. 2) erroneously conceived the notion that the lending of cheap money to farmers was "a

proper function of the government," while the Senate (53 Cong. Rec. 7246) thought that the act could not be saved except by adding a *"slight or insignificant"* provision giving the government the *privilege,* if and when desired, of using the agencies created as government depositaries, a subject hereinafter more particularly noticed (*Infra,* Div. V, subd. 6th).

V.

The Act cannot, as contended by Ex-Secretary McAdoo and Ex-Attorney General Wickersham, be sustained on the theory of the Joint Stock Banks, that it was an exercise of the power to establish agencies to perform necessary and essential governmental functions.

As heretofore stated, counsel for the Joint Stock Banks erroneously *assume* that these agencies, like the national banks, exercise *necessary* and *essential governmental* functions to which any *private* function is a mere incident. Counsel for the Land Banks, by placing the power solely on the right of appropriation, reject this contention. Counsel for the Joint Stock Banks base their view upon their erroneous assumption. Unless the agencies are, in the main, *governmental,* the reason for the rule invoked by them ceases, and when the reason ceases, the rule of law based thereon loses its force.

(1st) *Reasoning upon which the proposition advanced rests and its inapplicability here.*

This view, inconsistent with that of Ex-Justice Hughes, rests upon the thought that, although the Tenth Amendment reserved to the states all the powers not granted to the United States, yet since *general* banking was a *governmental* function, as distinguished from that which was *private,* Congress had, as was decided in *M'Cullough* v. *Maryland,* 4 Wheat. 316; *Osborn* v. *Bank,* 9 Wheat. 738, 792, *Farmers'* & *Mechanics' National Bank* v. *Dearing,* 91 U. S. 29, and *First National Bank* v. *Union Trust Co.,* 244 U. S. 416, known as the National Bank Cases, the implied power to establish such banks, even though coupled therewith and as an *incident* thereto, *private* functions were also exercised. The evident reason a great lawyer, like Ex-Justice Hughes, does not rely upon so simple a proposition, is the difficulty in assuming here that the act ever created *banks* or agencies, the *main* purpose of which was to perform *governmental* functions. With the premise gone, the proposition must fall.

(2d) *The main function of the agencies created was to deal with and for private and proprietary interests, not to perform a governmental service.*

(a) Here arises the real question in the case. If the *agencies* established were not, in fact, *general* banks, or, regardless of what they were, if their *main* purpose was *not* to exercise *necessary* and *essential governmental* functions, to which *private* business was a mere incident, the

premise on which the proposition rests wholly fails. *South Carolina* v. *United States,* 199 U. S. 437, and the National Bank Cases, when properly applied, are conclusive authorities in support of this view.

The fact a lawyer like Ex-Justice Hughes finds the power to exist in the right of appropriation, not in the exercise of any *real* governmental function, is an argument which strongly condemns the position of the Joint Stock Banks. Congress found the *same* power to establish *both* Land and Joint Stock Banks. This is, at least, persuasive that the power attempted to be exercised was not that of appropriation, for no money was advanced to the latter. The mistake that Congress made was, however, in erroneously assuming (53 Cong. Rec. 7246) that it was sufficient if the act permitted the agencies, if and when called on, to exercise governmental powers, "however *slight or insignificant,*" or that farm lending was (64 Cong. 1 Sess. Report No. 630, p. 2.) "a proper function of the government."

(b) "A mere *possibility*" that either of the alleged banks *might,* under section 6, be *unnecessarily* used in the future for some minor governmental purpose does not make it "an agency of the United States." This is conclusively settled by *Baltimore Ship Building Company* v. *Baltimore,* 195 U. S. 375, 382. Such an agency, in addition to being more than a *possibility* (id.), must have a "real or *substantial* connection" (Second Employers' Liability Cases, 223 U. S. 1) with the exercise of governmental functions. Other-

wise its existence, under *congressional* authority, cannot be justified. Moreover, the agency must be *necessary* and *essential* to aid the government in performing governmental duties, for, in *M'Cullough* v. *Maryland,* 4 Wheat. 316, Mr. Chief Justice Marshall remarked:

> "A bank to the government is a convenient, a useful and *essential* instrument in the prosecution of its fiscal operations. * * *"

Later (*Osborn* v. *Bank,* 9 Wheat, 738, 863) he said that it must be

> "* * * an instrument which is *necessary and proper* for carrying on the fiscal operations of government."

If the act does not measure up to these requirements, as it does not, it cannot stand. This precise question is settled by *M'Cullough* v. *Maryland* (4 Wheat. 316, 423), where Mr. Chief Justice Marshall said:

> "Should Congress, *under the pretext of executing its powers,* pass laws for the accomplishment of objects *not* entrusted to the government, it would become the painful duty of this tribunal, should a case requiring such a decision come before it, to say that such an act was not the law of the land."

So in *Osborn* v. *Bank,* 9 Wheat. 738, 860, 861, the same great jurist remarked:

> "The bank is not considered as a *private* corporation, whose *principal* object is indi-

> vidual trade, and individual profit; but as a public corporation, created for *public* and *national* purposes. That the mere business of banking is, in its own nature, a *private* business, and may be carried on by individuals or companies having no political connection with the government, is admitted; but the bank is not such an individual or company. It was not created for its *own* sake, or for *private* purposes. *It has never been supposed that Congress could create such a corporation.* * * * Why is it that Congress can incorporate or create a bank? * * * It is an instrument which is *'necessary and proper'* for carrying on the *fiscal operations of government."*

In *Farmers' & Mechanics' Bank* v. *Dearing,* 91 U. S. 29, 33, Mr. Justice Swayne said:

> "The national banks organized under the Act are instruments *designed* to be used to *aid the government* in the administration of an important branch of the *public* service."

Mr. Chief Justice White, in *First National Bank* v. *Union Trust Co.,* 244 U. S. 416, 425, from a review of the National Bank Cases, concluded:

> "What those cases established was that although a business was of a *private* nature and subject to state regulation, if it was of such a character as to cause it to be *incidental* to the *successful* discharge by a bank chartered by Congress of its *public* functions, it was competent for Congress to give the bank the power to exercise such *private* business *in co-operation with* or *as part of its public authority."*

(c) It is manifest that the act, as an exercise of *governmental* power, cannot stand if the agencies organized to carry it out, whatever called, did not, in the *main,* exercise *necessary* and *essential* governmental functions, and not those strictly of a *private* character, nor those which were incidental, non-essential and unnecessary. There cannot be ignored the difference (*South Carolina* v. *United States,* 199 U. S. 437, 461, 463) between "the scope and character of * * * *governmental* and *private* powers." Congress could not (*Infra* subd. 5th), as it attempted, provide for a farm loan system by giving the *name* of banks to simple loan agencies, and *calling* them, regardless of their actual character, "instrumentalities of government." Otherwise, form could override substance. The claim of power must, therefore, rest on the fact that the act *really* established *general* banks, as it does not, or agencies, the *main* functions of which were *governmental,* and the *private* business to be done only an incident thereto. If the *main* functions of the agencies established were simply to perform *private* and *proprietary* acts, as distinguished from those which were *governmental,* and the latter were merely *possibilities* or *incidental* to the others, then no power existed.

The National Bank Cases rested upon this sole theory of the exercise of governmental functions. Banks, the power to establish which is implied, within the meaning of the rule of these cases, must be *real* banks which, in the *main,* perform real and substantial *governmental* functions. This

must be, not a mere incident to, but the *main*, not a *minor*, object of their existence. The exercise of *private* powers must come solely as an incident (*First National Bank* v. *Union Trust Co.*, 244 U. S. 416) to the *main* purpose. As it is with *incidents* to interstate commerce, there must be "a real or *substantial* connection with" the *main* public function (*Second Employers' Liability Cases*, 223 U. S. 1).

(3d) *The National Bank Cases, when properly applied, sustain the contention of appellants.*

(a) The First and Second Banks of the United States were in fact *the means actually used* by the government to carry on all its fiscal operations, obtain loans in anticipation of revenue, facilitate the payment of federal taxes, furnish a uniform and orderly currency on a sound specie basis, collect, safeguard and transport money, and transfer public funds from place to place (without cost to the government or loss to it on account of the difference in exchange) as the exigencies of the nation required. (*M'Culloch* v. *Maryland*, 4 Wheat. 316, 407, 409; *Osborn* v. *Bank*, 9 Wheat. 738, 861, 864; Beveridge's Life of John Marshall, Vol. 4, pp. 171, 176, 195; Holdsworth & Dewey's First and Second Banks of the United States; McMaster's History of the People of the United States, Vol. 2, p. 29; *id.*, Vol. 4, p. 280 *et seq.*; especially pp. 300-318; Hamilton's Report on a National Bank.)

The appropriateness, as well as the absolute *necessity* for the Second Bank of the United

States as a national agency, arose from the fact that there was utter chaos in banking, the government had been deprived of its almost indispensable fiscal agent (the First Bank of the United States), and could not negotiate loans, taxes were collected with great difficulty, loss and delay, and the Treasury was so near bankrupt that the Department of State did not have sufficient money to pay its stationery bill. In desperation, the Treasury exchanged six per cent government bonds for the notes of state banks, thereby losing $5,000,000 from worthless bank bills. The local state banks became the sole depositaries for government funds. Their worthless currency flooded the country, interfering with commerce and all business, while the suspension of specie payments by them rendered a uniform national currency indispensable. (Lincoln's Veto Message of June 23, 1862, Six Messages and Papers of the Presidents, pp. 87, 88; Lincoln's Second Annual Message, Dec. 1, 1862; *id.*, pp. 126, 129-130; Rhodes' History of the United States, Vol. 4, pp. 237-239; Noyes' History of the National Banking Currency, p. 41; Davis' The Origin of the National Banking System, pp. 79, 80, 89, 106, 109; *Veazie Bank* v. *Fenno*, 8 Wall. 533, 536-539, 548.)

(b) The foregoing authorities also teach that the National Banking System was established, and was *in fact used* by the government, in order to furnish a sound and uniform currency and prevent injurious fluctuations thereof, facilitate the payment of troops, receive and distribute public subscriptions, provide a market for government bonds which were used as the basis of the notes

issued by the banks, and furnish convenient depositaries for public funds. This at a time when every collector of federal taxes feared to deposit the money in state banks, was responsible for the funds collected and yet was compelled to hold it in his personal possession, subject to the danger of fire and accident, the government not even furnishing an office safe for that purpose.

(c) The reasons for the establishment of national banks to perform the necessary and essential *governmental* functions clearly show that neither the Land nor the Joint Stock Banks were created as agencies for such purposes. Unless they were, there is not authority in Congress to establish them (*Osborn* v. *Bank,* 9 Wheat. 738, 860). The fact that unnecessarily they *may* possibly, if and when desired, be called upon to perform a *minor* governmental function is not sufficient (*Infra,* subd. 6th). Banks are not unknown things. They are capable of being and have frequently been defined. The very definition, so far as concerns the exercise of a *governmental* function, is well understood. The agencies provided for, though so-called, were not banks at all. Their *main* purpose was intended to be and in fact was to do business of a *private* and *proprietary* character. The *governmental* functions, if any, were only *minor,* and unnecessary, and at most *incidental* to the *main* purpose. They were, by sections 13, 14 and 16 of the Act, *prohibited* from engaging in banking. Even without that specific prohibition, they never could be properly classed as *banks.* So say the authorities. (3 Encyclopedia of the United

States Supreme Court Reports, pp. 5-7; *Bank for Savings* v. *Collector*, 3 Wall. 495, 512; *Oulton* v. *Savings Institution*, 17 Wall. 109; *Warren* v. *Shook*, 91 U. S. 704; *Selden* v. *Equitable Trust Co.*, 94 U. S. 419; *Knickerbocker Life Ins. Co.* v. *Pendleton*, 115 U. S. 339; *Mercantile National Bank* v. *New York*, 121 U. S. 138, 156; *Guthrie* v. *Harkness*, 199 U. S. 148, 157). Whenever there is any kind of congressional power to establish banks, the plain meaning is that those established must be institutions, the *main*, not the minor, purpose of which is to exercise *governmental* functions. Coming still closer to this case, it may be said that agencies like Land and Joint Stock Banks, prohibited from doing a banking business (secs. 13, 14, 16), are not banks, the *main* purpose of which is to exercise *governmental* functions, for, as has been (*State* v. *Reid*, 125 Mo. 43, 52) even said, "the mere fact that a corporation is authorized to exercise *some* of the functions of a bank does not, in law and in fact, create it a bank within the meaning of * * * law."

In 3 Encyclopedia of the United States Supreme Court Reports, pp. 5-7, it is stated:

> "And trust companies are not banks in the commercial sense of the word * **. The business of the stock broker is ordinarily distinct from the business of a banker, or according to the common understanding, is not a banker."

In *Selden* v. *Equitable Trust Co.*, 94 U. S. 419, 423, a corporation which, exactly as the Land and Joint Stock Banks do, loaned its own money on

notes secured by mortgages and sold these securities with its guaranty, using the proceeds to make other loans, was held not to be a "bank," Mr. Justice Strong pointedly saying:

> "The Equitable Trust Company lent its own money, taking bonds and mortgages therefor. Those bonds it sold with a guaranty. It sold only its own property, not that received from other owners for sale. Such a business, in our opinion, did not constitute the corporation a banker, as defined by the revenue laws."

In *Mercantile National Bank* v. *New York*, 121 U. S. 138, 159, Mr. Justice Matthews aptly put it:

> "Trust companies * * * are not, *in any proper sense* of the word, banking institutions. * * * are not banks in the commercial sense of that word, and do not perform the functions of banks in carrying on the exchanges of commerce."

This doctrine was restated and applied in *Jenkins* v. *Neff*, 186 U. S. 230. In *Wells Fargo & Co.* v. *Railroad*, 23 Fed. Rep. 469, an express company did far more of the ordinary business done by a bank than can be done by a Land or Joint Stock Bank, yet it was, upon unanswerable reasoning, held not to be a bank. So, in a somewhat similar case, it was said as to a savings association (*State* v. *Louisiana Savings Co.*, 12 La. Ann. 568). Substantially, the same rulings (*Loan & Trust Co.* v. *Helmer*, 77 N. Y. 64; *Pratt* v. *Short*, 79 N. Y. 437; *People* v. *Railroad*, 12 Mich. 390; *State* v.

Granville Alexandrian Society, 11 Ohio 1; *State* v. *Stebbins*, 1 Stewart (Ala.) 299; *State* v. *Reid*, 125 Mo. 43; *State ex inf.* v. *Lincoln Trust Co.*, 144 Mo. 562), have been applied to many other like corporations. Probably the best detailed and most extended review of the cases is found in *State* v. *Reid*, 125 Mo. 43, a careful reading of which will probably satisfy any inquiring mind that neither a Land nor a Joint Stock Bank is, in any sense, a bank, the *main* purpose of which is to perform some *governmental* function, and to which any *private* power exercised is a mere incident (*Osborn* v. *Bank*, 9 Wheat. 738, 860; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416, 425). Such an agency has not "any real or substantial connection" (Second Employers' Liability Cases, 223 U. S. 1) with the exercise of any *governmental* function. Instead of the *private* powers being an *incident* to those which are *governmental*, the few *minor* governmental powers which are *possible* to be exercised are unreal, unsubstantial, unnecessary, non-obligatory, and merely *incidental* to the exercise of those which are strictly *private* and *proprietary*.

(4th) *The fact that the government may have loaned or advanced money to either agency does not convert the functions of the latter from private to governmental.*

(a) All the powers of a state or the United States are either *governmental* or else *private* and *proprietary*. These two classes of powers are well defined, quite *distinct* and fully recognized (*South Carolina* v. *United States*, 199 U. S. 437, 461, 462; *First National Bank* v. *Union Trust Co.*,

244 U. S. 416; *Illinois Trust & Savings Bank* v. *Arkansas City*, 76 Fed. Rep. 271, 282, 22 C. C. A. 171). In the South Carolina case (199 U. S. 437, 461, 463), Mr. Justice Brewer reviewed the decisions and concluded as to such powers there was a marked distinction between "those which are of a strictly *governmental* character," and "those which are used * * * in the carrying on of an ordinary *private* business." He then concluded:

> "Now, if it be well established, as these authorities say, that there is a clear distinction as respects responsibility for negligence between the powers granted to a corporation for governmental purposes and those in aid of private business, a like distinction may be recognized when we are asked to limit the full power of imposing excises granted to the national government by an implied inability to impede or embarrass a state in the discharge of its functions. It is reasonable to hold that, while the former may do nothing by taxation in any form to prevent the full discharge by the latter of its governmental functions, yet, whenever a state engages in a business which is of a private nature, that business is not withdrawn from the taxing power of the nation."

The learned justice adopted, as applicable to the government, the distinction as to the *governmental* and *private* powers of a city. Of these, in the Arkansas City case (76 Fed. 271, 282, 22 C. C. A. 171), Judge Sanborn said:

> "A city has two classes of powers—the one legislative, public, governmental, in the

exercise of which it is a sovereignty and governs its people; the other proprietary, *quasi*-private, conferred upon it, not for the purpose of governing its people, but for the private advantage of the inhabitants and of the city itself as a legal personality. In the exercise of the powers of the former class it is governed by the rule here invoked. In their exercise it is ruling its people and is bound to transmit its powers of government to its successive sets of officers unimpaired. But in the exercise of the powers of the latter class it is controlled by no such rule, because it is acting and contracting for the private benefit of itself and its inhabitants, and it may exercise the business powers conferred upon it in the same way, and in their exercise it is to be governed by the same rules that govern a private individual or corporation. * * * In contracting for waterworks to supply itself and its inhabitants with water, the city is not exercising its governmental or legislative powers, but its business or proprietary powers. The purpose of such a contract is not to govern its inhabitants, but to obtain a private benefit for the city itself and its denizens."

In *Bank of United States* v. *Planters Bank*, 9 Wheat. 904, 907, 908, Mr. Chief Justice Marshall outlined the same view by saying:

"* * * when a government becomes a partner in any trading company, it divests itself, so far as concerns the transactions of that company, of its sovereign character, and takes that of a private citizen. Instead of communicating to the company its privileges and its prerogatives, it descends to a level

with those with whom it associates itself, and takes the character which belongs to its associates, and to the business which is to be transacted. * * * As a member of a corporation, a government never exercises its sovereignty. It acts merely as a corporator, and exercises no other power in the management of the affairs of the corporation, than are expressly given by the incorporating act.

The Government of the Union held shares in the Old Bank of the United States; but the privileges of the government were not imparted by that circumstance to the bank. * * * The government, by becoming a corporator, lays down its sovereignty, so far as respects the transactions of the corporation, and exercises no power or privilege which is not derived from the charter."

In *Flint* v. *Stone Tracey Co.*, 220 U. S. 107, 172, in denying an attempt by a state to withdraw from the federal taxing power, corporations of a public nature, Mr. Justice Day said:

"It is no part of the *essential* governmental functions of a state to provide means of transportation, supply artificial light, water and the like. These objects are often accomplished through the medium of *private* corporations, and though the public may derive a benefit from such operations, the companies carrying on such enterprises are, nevertheless, *private* companies, whose business is prosecuted for *private* emolument and advantage. For the purpose of taxation they stand upon the same footing as other *private* corporations upon which special franchises have been conferred. The true distinction is between the attempted taxation of those operations of the

states *essential* to the execution of its governmental functions, and which the state can only do itself, and those activities which are of a *private* character."

(b) It follows that the money which the government advanced to the Land Banks as a *loan* to make the initial stock payment, did not convert the scheme into one of a *governmental* nature.

(5th) *The fact that the agencies provided were actually named banks, or called instrumentalities of the government, does not prevent an inquiry into the unquestionable fact that they were not in reality such.*

This because mere words or forms cannot be used to evade a plain constitutional mandate. The calling of a corporation a bank, or an instrumentality of the government, when, in fact, it is not such, cannot justify the exercise of a power forbidden by the constitution. This is what Mr. Justice Harlan had in mind when he, in *Western Union Telegraph Co.* v. *Kansas,* 216 U. S. 1, 27, said:

> "This court has repeatedly adjudged that in all such matters the judiciary will not regard mere forms, but will look through forms to the substance of things. Such is an established rule of constitutional construction, as the adjudged cases abundantly show. * * * In *Mugler* v. *Kansas,* 123 U. S. 623, it was said that the courts, when determining whether a statute is consistent with the fundamental law, must not deem themselves 'bound by mere forms, nor are they to be misled by mere pretenses. They are at liberty—indeed, are

> under a solemn duty—to look at the substance of things, whenever they enter upon the inquiry whether the legislature has transcended the limits of its authority.'"

In the same case, Mr. Justice Holmes (p. 55) recognized the same principle by saying:

> "I hardly can suppose that the provision is made any the worse by giving a bad reason for it or by calling it by a bad name. I quite agree that we must look through form to substance."

In *Mugler* v. *Kansas,* 123 U. S. 623, 31 L. Ed. 205, 210, Mr. Justice Brewer had previously expressed the idea in these words:

> "The courts are not bound by mere forms, nor are they to be misled by mere pretenses. They are at liberty—indeed, are under a solemn duty—to look at the substance of things, whenever they enter upon the inquiry whether the legislature has transcended the limits of its authority. If, therefore, a statute purporting to have been enacted to protect the public health, the public morals, or the public safety, has no *real* or *substantial* relation to those objects, or is a palpable invasion of rights secured by the fundamental law, it is the duty of the courts to so adjudge, and thereby give effect to the Constitution."

The same principle has been so frequently announced in other cases that it may be said to be a settled doctrine of this court.

In *Henderson* v. *Wickham,* 92 U. S. 259, 268, 23 L. Ed. 543, 547, Mr. Justice Miller said:

> "In whatever language a statute may be framed, its purpose must be determined by its natural and reasonable effect; and if it is apparent that the object of this statute, as judged by that criterion, is to compel the owners of vessels to pay a sum of money for every passenger brought by them from a foreign shore and landed at the port of New York, it is as much a tax on passengers if collected from them, or a tax on the vessel or owners for the exercise of the right of landing their passengers in that city, as the statute held void in the Passenger Cases."

In *Robbins* v. *Taxing District,* 120 U. S. 489, 30 L. Ed. 694, 697, Mr. Justice Bradley remarked:

> "The mere *calling* of the business of a drummer a privilege cannot make it so."

In *Smith* v. *St. L. & S. W. R. Co.,* 181 U. S. 247, 257, 45 L. yd. 847, 851, Mr. Justice McKenna said:

> "Any pretence or masquerading will be disregarded and the true purpose of a statute ascertained."

In *Stockard* v. *Morgan,* 185 U. S. 27, 36, 46 L. Ed. 785, 794, Mr. Justice Peckham said:

> "The fact that the state or the court may *call* the business of an individual, when employed by more than one person outside of the state to sell their merchandise upon a commission, a 'brokerage business,' gives no au-

thority to the state to tax such a business as complainants. The *name does not alter the character of the transaction,* nor prevent the tax thus laid from being a tax upon interstate commerce."

In *Reid* v. *Colorado,* 187 U. S. 137, 151, 47 L. Ed. 108, 115, Mr. Justice Harlan said:

"Certain principles are well settled by the former decisions of this court. One is that the purpose of a statute, in *whatever* language it may be framed, must be determined by its natural and reasonable effect."

In *Galveston H. & S. A. R. Co.* v. *Texas,* 210 U. S. 217, 227, 52 L. Ed. 1031, 1037, Mr. Justice Holmes said:

"Neither the state courts nor the legislatures, by giving the tax *a particular name or by the use of some form of words,* can take away our duty to consider its nature and effect. If it bears upon commerce among the states so directly as to amount to a regulation in a relatively immediate way, it will not be saved by *name* or *form.*"

In *St. L. S. W. R. Co.* v. *Arkansas ex rel. Norwood,* 235 U. S. 350, 363, it was by Mr. Justice Pitney said:

"But when the question is whether a tax imposed by a state deprives a party of rights secured by the Federal Constitution, the decision is not dependent upon the *form* in which the taxing scheme is cast, nor upon the *characterization* of that scheme as adopted

> by the state court. We must regard the *substance,* rather than the form, and the controlling test is to be found in the operation and effect of the law as applied and enforced by the state."

In *Mountain Timber Co.* v. *Washington,* 243 U. S. 219, 237, Mr. Justice Pitney said:

> "The question whether a state law deprives a party of rights secured by the Federal Constitution depends not upon how it is *characterized,* but upon its practical operation and effect."

(6th) *The attempt by section 6 to provide for possible service to the government was a subterfuge and merely a scheme to evade the Constitution.*

(a) Notwithstanding the official pronouncements hereinbefore set out (*Supra,* subd. 2d), Congress went into that which has (Atlantic Monthly, 222, 225, February, 1917) been termed "the *private* business of lending money for agricultural purposes." The Joint House and Senate Committee found the power (53 Cong. Rec. 453, 489, Report No 630, 64th Cong., 1st Session) to pass the act by conceiving the mere lending of money to farmers to be *governmental* in its nature. The Senate resorted to a mere pretense. Of this there is not a shadow of doubt. Some of the ablest senators opposed its passage in elaborate arguments (53d Cong. Rec., pp. 6961, 6965, 6968, 7245, 7246, 7305, 7317) well worthy of perusal. Senator Hollis, who had charge of the

bill, and many of its principal advocates had such grave doubts of its constitutionality that they openly admitted the necessity of adding to it (*id.*, pp. 6861, 7026, 7129, 7246, 7310) the minor *incidental* feature that the government should have the *non-essential* and *unnecessary* privilege (section 6) to use, *if* and when desired, the agencies created, as government depositaries and financial agencies. By adding such features, even in *optional* form and as a mere *possibility*, it was assumed (in the face of the principle established in *Baltimore Ship Building Co.* v. *Baltimore*, 195 U. S. 375, 382) that the agencies would, like the national banks, exercise banking or governmental powers. This notwithstanding that sections 13, 14 and 16 expressly provided that no one of them should "have power to transact any banking business," and that Joint Stock Banks should receive deposits from *no one* and Land Banks *only* "from its own stockholders." This plainly appears, for Senator Hollis, doubting the constitutionality of the proposed act, thus (53 Cong. Rec. 7026) called for help from his brother senators:

> "MR. HOLLIS: The constitutional features of the bill have *given me great concern* * * *. The Democratic, Republican and Progressive platforms declared for rural credits. Therefore, we must do the best we can. If any friend of the bill can think of any other feature that should be added to it to make the bill *surely* constitutional, I would very gladly welcome it. I hope the senator from South Dakota and other friends of the measure will address themselves to that matter, and if they find anything further, will inform the Senate."

After hearing the *various* suggestions of many, Senator Cummins (53 Cong. Rec. 7246) came to the rescue of Senator Hollis with this suggestion:

> "MR. CUMMINS: In this case, however, the *chief* purpose of the corporation, as avowed by all who have spoken on its behalf and as I think will be admitted by everybody, is to secure a lower rate of interest to those who borrow from the Land Banks; that is its *only* object. It is necessary, however, to find some governmental purpose, *however slight or insignificant*, in order to invoke the authority of Congress in the incorporation, and, therefore, it is declared that these land banks shall be public depositaries * * *."

(b) The mere right to designate the banks as government depositaries and financial agents is not the main purpose of the scheme, but, at most, was, if not a pure device, a mere minor incident thereto, wholly *unnecessary and non-essential.*

Section 6 of the act provides:

> "That all Federal Land Banks and Joint Stock Land Banks organized under this act, *when designated for that purpose* by the Secretary of the Treasury, shall be depositaries of public money, except receipts from customs, under such regulations as may be prescribed by said Secretary; and they may *also be employed* as financial agents of the Government; and they shall perform all such reasonable duties, as depositaries of public money and financial agents of the Government, *as may be required of them.* And the Secretary of the Treasury shall require of the Federal Land Banks and Joint Stock Land Banks thus

> designated satisfactory security, by the deposit of United States bonds or otherwise, for the safekeeping and prompt payment of the public money deposited with them, and for the faithful performance of their duties as financial agents of the Government. No Government funds deposited under the provisions of this section shall be invested in mortgage loans or farm loan bonds."

This section is that "small or insignificant" provision which Senator Cummins (53 Cong. Rec. 7246) erroneously assumed would make valid that which otherwise would be unconstitutional. It was a makeshift, a pretense, and a mere subterfuge. It merits the condemnation thus pronounced (119 Atlantic Monthly 222, 231) by Governor Herrick:

> "This combination of government finance and farm finance defies every construction of the Constitution save the broadest. Congress cannot exempt a corporation from the taxing powers of the states or of their political divisions, except for discharging a federal government function. Farm-mortgaging is not such a function. The framers of the system, however, declare that this will be its chief object, and they pretend that the land banks were authorized to be designated as depositaries and financial agencies of the government, and that their bonds and mortgages were made the government's instrumentalities, simply with the view of getting around constitutional objections. But the Supreme Court has said in regard to *subterfuges* of this kind and their use for a private corporation that 'The casual circumstance of its being employed

> by the government in the transaction of its fiscal affairs would no more exempt its *private* business from the operation of that power (of the state to tax) than it would exempt the private business of any individual employed in the same manner.' Moreover, the court has even doubted that Congress has a right to establish or to privilege a company in any way 'having private trade and private profit for its great end and principal object,' or to delegate the power which it possesses under the Constitution 'to borrow money on the credit of the United States.'"

The quotations thus used by Governor Herrick were from *Osborn* v. *Bank*, 9 Wheat. 738, 859, 860.

(c) The section does not *require*, but only *permits*, the banks to be designated as depositaries of public money and their employment as financial agents of the government. They, in such capacities, are not *required* to perform duties. They are to perform only such as *may* be required of them. The law made no such designation nor any such requirement. Both agencies might *forever* exist without either of them ever being so designated or employed. All government funds, *if* deposited in any such depositary or financial agency, must be kept separate and apart from any other funds *and cannot be invested in farm mortgages or bonds.*

It is wholly immaterial that some artful mind may have suggested, as indicated by Senator Cummins (53 Cong. Rec. 7246), the insertion of this section to give to the scheme a color that *governmental* functions were to be performed. It is

sufficient to say they were not the *main* purpose of the scheme. If anything, they were *possibilities*, and if availed of, mere *incidents*, wholly *non-essential* and *unnecessary* to the *main* purpose. That *main* purpose was to obtain from *private* persons *private* money to loan for the *private* use of one class and the *private* gain of another.

(d) This view accords with the practical working of thte Act. The bill (Rec. 10) avers that none of the *alleged banks*, Land or Joint Stock, has ever engaged in the banking business. It also avers that neither has been made a government depositary or financial agent, nor ever accepted any government deposits, *except that during the summer of 1918*, the Land Banks at Wichita, St. Paul and Spokane were *temporarily* designated as *financial agents* of the government for the *sole* purpose of making seed grain loans to drought-stricken farmers. The President, at the request of the Secretary of Agriculture, set aside, out of his $100,000,000 of *war* funds, $5,000,000 for that purpose. These three banks made upwards of fifteen thousand seed loans, aggregating $4,500,000, all secured by crop liens. In making these loans, the three banks acted without compensation. This, under a joint circular of the Treasury and Agricultural Departments, which allowed actual expenses but no more (Bill, Rec. 10). No Joint Stock Bank was ever so used, even temporarily. This affirmatively shows that the section as to the agencies was wholly unnecessary and their designation, if ever made, wholly non-essential. It would seem to be absurd to say because of the mere *privilege* to so designate Land and Joint Stock

Banks the *main* purpose of the act was *governmental.* Moreover, to say that the *government* has this right, as a mere *privilege,* is to admit that neither bank is a *necessary* and *essential* governmental agency. The mere *possibility* that at some *future* time the United States *may* elect to designate a Land or Joint Stock Bank as a depositary and thereafter *may further elect* actually to use it as such, while in the meantime the corporation is engaged solely in *private* business for *private* gain, certainly does not make it such a government instrumentality as will exempt it from state taxation, or authorize Congress to create it. *Baltimore Ship Building Co.* v. *Baltimore,* 195 U. S. 375, 382, is, in principle, decisive. There Mr. Justice Holmes, among other things, said:

> "It would be a very harsh doctrine that would deny the right of the states to tax lands because of a *mere possibility* that they might lapse to the United States."

(e) The agencies did not become *governmental,* simply because they *might* be designated as *depositaries* and *financial* agents. So many of such depositaries existed that this permission, had the Act, instead of making it *possible, absolutely* named the *alleged* banks as such, would have been a *minor* matter and could not be said to have been its *main* purpose. The Treasury Annual Reports 1919, Finance 722, as to government depositaries states:

> "The Secretary of the Treasury determines the *number* of such depositaries. The regular depositaries receive and disburse the public

moneys, while the *special* depositaries hold only the moneys transferred from the Treasury. The number of national depositaries (*excluding special depositaries appointed under the Liberty Loan Acts*) at the close of the fiscal years 1918 and 1919 are here stated:

Depositaries	Regular	Special	Total
June 30, 1918.....	765	3624	3389
June 30, 1919.....	807	645	1452"

Again in the same volume (*id.*, p. 112), it is said:

> "At the beginning of the fiscal year of 1919 there were 6,510 special depositaries and at the close of the year there were 9,550, of which 4,510 were national banks and 5,039 state banks and trust companies. Both national and state banks were designated as such depositaries in every state in the Union."

With so many depositaries already existing and ample power in a department merely for the asking to create more, it would be absurd to say that this permission given in section 6 was, in itself, so *essential* that it was the *main* feature of the act.

VI.

The passage of the Act cannot, as contended for by the Land Banks, through Ex-Justice Hughes, be sustained as an exercise of the power to appropriate the public money for public purposes.

One cannot be unmindful of the force of any view presented by such a lawyer as Ex-Justice

Hughes, nor ignore the importance thereof. He is himself an authority. It is, therefore, no light task to oppose him, especially when his position has been taken after thorough study. It might be different if the suggestion were made by someone less eminent.

(1st) *The question.*

(a) This contention is practically this:

> *Express* provision is made in the constitution (Art. I, sec. 8, clause 1) that "Congress shall have power to levy and collect taxes * * * and provide for the common defense and general welfare of the United States." *Express* power being thus clearly given to levy and collect taxes, implies the power to spend the money collected. Agriculture is a matter of national concern. Whatever tends to assist or to develop it contributes to the "general welfare." The lending of money to farmers at low interest rates is a benefit to the agricultural interests. Hence Congress can "provide for the * * * general welfare" by appropriating money in order to lend it to farmers at such low rates.

This *same* principle, if sound, would permit the government to do *anything* deemed for the general good. It would support appropriations made for the benefit of manufacturers, miners, wage earners, the aged poor and unemployed, or to those engaged in educating the youth of the land. This, too, by the activities carried on by corporations, the *chief* purpose of which was to loan money in a *private* business in *unlimited* amounts for *unlimited periods* of time, even *after* the government's

advance had been returned to it. Such a use of the *general welfare* clause is in the face of *Kansas* v. *Colorado* (206 U. S. 46), which distinctly holds that the *power* must be found in some other clause before the states can be deprived of those *internal rights* (*Supra,* Div. II) otherwise expressly reserved to them by the Tenth Amendment. It is also against the doctrine of *Osborn* v. *Bank,* 9 Wheat. 739, 859, that Congress cannot under it create a bank, the functions of which are in the *main* of a private nature.

(b) Assuming, even if it be possible in a proper case for Congress, under the power of appropriation to give or lend the public money to any *class,* the question here involved is *not* as to any public money *appropriated,* nor the protection or investment thereof, nor the *possible* power of Congress to make appropriations and carry them out through corporations of its own creation. The real questions are, *first,* whether it can create and forever control *private* investment corporations doing, in the *main,* a *private business,* without limit in the amount of their investments or the period of their existence; *second,* exempt from state taxation, not the *public* money appropriated for their benefit or loaned to them, but *all* their corporate assets and all the *private* investments of *private* investors in their securities, and, *third,* then, even after the public money is exhausted or repaid, continue the ordinary *private* business of dealing, for a profit, in farm mortgages or bonds secured thereby.

(2d) *The view advanced is a wholly new discovery and differs entirely from that of Congress (Infra, subd. 3d), the courts (Infra, subd. 5th), the legal profession (Infra, pars. [b], [c]), the advocates of and sponsors for the Act (Infra, subd. 4th), and the principles upon which the National Bank Cases rest (Infra, subd. 5th).*

(a) The view advanced was at great length and with much vigor set forth in a printed opinion of Ex-Justice Hughes on May 4, 1917 (*Supra*, Div. II, subd. b), which was used by bond sellers in disposing of the Land Bank bonds. Long *thereafter*, in 1918 and 1919, Ex-Secretary McAdoo and Ex-Attorney General Wickersham and *many* other leading members of the profession declined to follow this opinion. They furnished (*Supra*, Div. III, subd. a) their *own* opinions to the sellers of Joint Stock Bank bonds. These found, and had to find, in order to sustain such bonds, the power to exist on the very *different* claim that Congress could provide and had provided for agencies to perform *governmental* functions. It is at least significant that these eminent counsel were at the time fully advised of the position of Ex-Justice Hughes, with which they did not agree.

(b) Never before in our history was it *suggested* that the power to create a corporation to do a *private* business could be deduced from the power to appropriate public money. The United States subscribed largely to the capital stock of both the First and Second Banks of the United States. But neither Alexander Hamilton, Daniel Web-

ster, nor Mr. Chief Justice Marshall suggested that the *congressional* creation of the bank could be sustained under the power of appropriation, which was then, as claimed here, exercised by a subscription to the bank's capital stock. With both Banks of the United States, the government's subscription was, however, absolute and *permanent*. Here it was *conditioned* on the public not *permanently* subscribing for the stock, but *temporarily* loaning some money, the advancements for which were to be returned and are now in the process of rapid retirement.

(c) Neither in the National Bank Cases (*M'Culloch* v. *Maryland*, 4 Wheat. 316; *Osborn* v. *Bank*, 9 Wheat. 738; *Bank* v. *Dearing*, 91 U. S. 29; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416) nor in the arid land case (*Kansas* v. *Colorado*, 206 U. S. 46), nor in the great cases concerning matters of *internal* concern (*Supra*, Div. II) was the thought ever advanced by any lawyer or justice that the power to establish and control the selected agencies to carry out a congressional act rested or could rest upon the right to appropriate *public* money.

(3d) *To so find the power would be contrary to the clear intent of Congress.*

(a) This is manifest from the simple fact that Congress assumed that *the same power* existed as to both classes of banks, though there was, and could be, no claim of an appropriation as to the Joint Stock Banks.

(b) In Congress the question of the constitutionality of the Act was thoroughly discussed (53

Cong. Rec. 6793, 6795, 6796, 6861, 7020, 7129, 7246, 7310) by lawyers of signal ability. No one of them ever entertained the thought that the act could be justified as an exercise of the power of appropriation.

(c) Upon the other hand, Congress justified it on the entirely *different* ground that it was to provide agencies, the functions of which were governmental.

There was never the slightest intention to make an appropriation. The Joint Committee of the Senate and House recommended the passage of the Act (55 Cong. Rec. 453, 489, 64 Cong., 1st Session, Report No. 630; Senate Report No. 144; House Document No. 494) because it was *conceived* that lending to farmers the money of *private* investors was "a proper function of the government." Senator Cummins said (53 Cong. Rec. 7246) that Congress, to make the act constitutional, deemed it necessary to insert the provision, however *"small or insignificant,"* authorizing the agencies to perform governmental functions by acting as government depositaries *if* and *when* called upon.

(d) It may, therefore, be emphatically asserted and repeatedly reasserted that Congress never intended by passing the Act to exercise any power of appropriation. Hence, to sustain it on any such ground would be to ignore the *real* purpose and intent of Congress.

(4th) *An attempt to invoke the power of appropriation is not only contrary to the intention of Congress, but is also against that which was*

by the sponsors and advocates of the Act declared to be its sole purpose.

No advocate or sponsor for the Act ever sought to justify it as an exercise of the power of appropriation. On the contrary, all such persons proceeded upon the theory that there would be no appropriation (*Supra*, Div. IV, subd. b). Of this, there is not the slightest doubt. The American Commission (63 Cong., 2d Session, Sen. Doc. 261, part 1, page 13) said that the scheme should "be worked out *without* government aid." The United States Commission (63 Cong., 2d Sess., Sen. Doc. 380, p. 22) reported that "it is wise legislation *rather than liberal appropriations*, which rural credit mostly needs at our hands." President Wilson (119 Atlantic Monthly 222) in his first annual message of December 2, 1913, stated:

> "The farmers, of course, ask and should be given no such privilege as extending to them the credit of the government itself."

Ex-Secretary McAdoo on a similar subject (119 Atlantic Monthly, 223) said:

> "* * * you ask us to stand for a proposition to *lend* money to *private* corporations or individuals upon the security of mortgage. Never on the face of the earth!"

Secretary Houston, when head of the Agricultural Department, in his report of 1914 (119 Atlantic Monthly, 222) said:

> "The chief difference of opinion arises whether there should be *special aid furnished*

> *by the government.* There seems to be no emergency which requires or *justifies* government assistance to the farmers directly through the use of the government cash or the government credit."

The Senate and the Joint House and Senate Committee on Rural Credits (64 Cong., 1st Sess., House Doc. 494, p. 6) reported:

> "The American farmer does not come to Congress with a hard luck story. He *does not ask* the government to *bestow* on him the *public* money that all the people have contributed for taxes."

The only purpose was, as declared in the congressional debates and the government literature (*Supra*, Div. IV, subd. b), and recognized by observing writers (119 Atlantic Monthly 222; 10 Lawyer and Banker and Southern Bench and Bar Review, October, 1917, p. 402) at the time, to obtain the *private* money of *private* investors to loan to farmers at *low* interest rates. The *chief, primary* and *sole* purpose of the Act was said by the House and Senate Joint Committee (64 Cong., 1st Sess., Report No. 630, p. 2) and Senators Hollis (53 Cong. Rec. 6793), Robinson (*id.* 7228) and Cummins (*id.* 7246) to be to create a system of *farm* lending. It is so recited in the Farm Loan Primer (p. 3), and so stated in the First Annual Report of the Federal Farm Loan Board pp. 13, 17, 22.

(5th) *The power to pass the Act as an appropriation measure is denied by the decisions here.*

(a) That which has already been said as to the *main* functions of the agencies (*Supra*, Div. V, subd. 2d) and the right of the court to look through mere forms and ignore all devices, pretexts and pretenses (*Supra*, Div. V, subd. 5th, 6th) is equally applicable where the power attempted to be exercised is that of appropriation. To say that the Act was *intended* to be or was passed as an appropriation measure is to deny the truth. To intimate that the *main* function of the agencies was to deal with an appropriation (*Supra*, subd. 2d) would be to countenance a mere pretense and makeshift in the face of the *intention* of the lawmakers to the contrary. To rest the authority to pass the Act on the power to appropriate money would be the merest pretext.

(b) From that which has already been said it may be safely asserted that unless the *functions* of the agencies were, in the *main*, to deal for the government with an *appropriation*, no subsequent *pretense* of so doing can make the Act valid. The *principal* purpose must have been to *appropriate* public money; the *private* business must have been incidental thereto (*Supra*, Div. IV, subd. 2d).

(c) *M'Culloch* v. *Maryland*, 4 Wheat. 316, 423, explicitly decided that if "under the *pretext* of exercising its powers Congress should attempt to pass a law to accomplish an object not intrusted to the government," the Act would be declared

unconstitutional. So in *Osborn* v. *Bank*, 9 Wheat. 738, 860, it was expressly held that "it has never been supposed that Congress could create" a corporation whose immediate purpose was to loan money. These two cases are controlling.

(6th) *Not only was there no intention of exercising any power of appropriation, but the Act, on its face, shows that none was exercised.*

The attempt to sustain the Act as an exercise of the power of appropriation could well rest here. If, however, substantial reasoning in its support could be applied or clearly and logically followed, the entire controversy would be narrowed to the two inquiries whether the Act *is* an appropriation measure, and, if so, whether the means adopted were, as they must be (*M'Culloch* v. *Maryland*, 4 Wheat. 316, 421; *Kansas* v. *Colorado*, 206 U. S. 46, 88; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416), appropriate to the end in view.

(a) A casual reading demonstrates that it is not, and, in fact, was never intended to be (*Supra*, Div. IV) an appropriation of money. Only *incidentally* is the public money used, and then only *temporarily* and as a means of accomplishing the real object of the legislation. In no sense is the use of public money *essential*, nor is it in any degree the *object* to be attained. The only appropriation is $100,000 (sec. 33) for the minor and purely incidental purpose of carrying into effect an Act which there is *supposedly* power to pass. If, within thirty days after the opening of sub-

scription books any part of the minimum capitalization of the Land Banks remains unsubscribed, the Secretary of the Treasury shall, on behalf of the government, subscribe for the balance (sec. 5, par. 5). Any money advanced for any such government stock shall be practically *as a loan*, repaid without interest. $6,000,000 of public money was authorized to be deposited in the Land Banks for their *temporary* use (sec. 32). These are the only references to public money, and upon these any claim of an appropriation must be based. Unquestionably the chief, primary and *sole* purpose of the Act is farm lending. The title, misleading as it is, shows that it is not an appropriation measure, but was by its framers only conceived to be one "to provide capital for agricultural development, to create standard forms of investment based upon farm mortgages, to equalize rates of interest upon farm loans, to furnish a market for United States bonds, to create government depositaries and financial agents for the United States and for other purposes." These words suggest no thought of an appropriation. Complete machinery was provided for accomplishing the ends in view. It was contemplated that it should, in the first instance, all be done without the use of a dollar of public money, except the necessary expenses of organization, and even they were to be repaid. Land Banks, Joint Stock Banks and Farm Associations were to be formed without financial assistance from the government, and, with the exception of Land Banks, must be formed without its assistance. In the one excepted case it was

provided that *if* the necessary stock subscriptions did not come from private sources, the government should subscribe the minimum balance, to be *repaid*, without interest or dividends, as rapidly as additional stock could be placed. This in effect was a simple loan, which was a *private*, not a *governmental*, matter (*Supra*, Div. V, subd. 4th). The legislation is perfect and complete in all its parts without an appropriation. The latter, even if it could be implied, is simply an *incident* designed to make the Act effective if other means should *temporarily* fail. The Act can no more be justified as the exercise of the power of appropriating public money than could one incorporating a national insurance or other *private* company, to which was attached a section providing that the government should subscribe for any stock *not* subscribed by individuals. That which it does is to provide *private* capital for *private* investment on *private* farm land security, the standardization of *private farm* mortgage investments and the equalizing of rates of interest on *private* farm loans. Some public money *may* temporarily be used to put the Act into operation. The immediate purpose and actual *intent*, however, was that all the organizations should function absolutely *without public money*. Every provision was expressly and adequately framed to accomplish that end. The plain truth is that the system created is one for conducting a *farm* loan business by *national* corporations under *national* control and regulations, free from state interference and from *any kind of taxation*, state or federal.

(b) Considered, however, as an appropriation measure, the means adopted are neither necessary nor proper to the end in view. Congress may, of course, adopt any proper means to accomplish a legitimate end. It can do no more (*M'Culloch* v. *Maryland*, 4 Wheat. 316, 421; *Kansas* v. *Colorado*, 206 U. S. 46, 88; *First National Bank* v. *Union Trust Co.*, 244 U. S. 416). The end to be accomplished by this legislation was not the development of agriculture or the stabilization of *farm* credits. No power to develop agriculture or stabilize farm credits can be found anywhere in the Constitution. It cannot rest under the general welfare clause, any more than could (*Kansas* v. *Colorado*, 206 U. S. 46) the power to reclaim arid lands. The legitimate, and only legitimate, end of the legislation is the spending of public money for the *private* business and *private* ends of a *particular class* of people. This is the end which must, if it can, justify the means. The apparent strength of any argument in favor of the power to pass the Act must be based upon the fundamentally erroneous deduction that the development of agriculture is within the general welfare clause, therefore a legitimate object of congressional appropriation; that being such a legitimate object, Congress may adopt any proper means to further it, and that the means under consideration are proper. This is a complete *non sequitur*. It might possibly be argued that, if a legitimate object of *congressional appropriation*, any means proper to *carry into effect such appropriation*, if made, may be adopted. Without discussing the question it may be said

that such a conclusion is untenable, for the means provided by the Act are not proper to the end in view. If Congress could *lawfully* appropriate $9,000,000 for the purpose of making loans to farmers, it is wholly unnecessary to consider whether it would be possible to create boards and corporations to handle such *public* funds and make therefrom such loans under suitable provisions. No such thing was attempted. Nor is it necessary to consider whether provisions *might* have been made for the continuous use of the money so appropriated by relending it when the original loans should be paid off. No such provisions were made. On the contrary, Congress provided for the organization of *private* corporations whose capital is to be subscribed in the first instance by *private* individuals and later by other *private* individuals organized into Farm Associations. It provided for these *private* corporations, raising additional funds by the sale to *private* individuals of tax-exempt bonds to be paid for by *private funds*. It provided expressly and necessarily that even such public money as might temporarily be used to put the system on its feet should be promptly and regularly repaid to the government *as fast as any business was done*. The machinery is especially arranged *not* to get *public* money *in*, but to keep *public* money *out* and to eliminate expeditiously any *public* money that may get in. No loan can be made by the Land Banks without a *private* subscription to their stock. This leads directly to the retirement of the government stock. The scheme cannot succeed without the speedy disappearance

of all *public* money therefrom. It was the evident purpose that no *public* money should be used, unless absolutely necessary, but that if any such were necessary, it should be as little in amount and for as short a time as possible. The means were admirably adapted to accomplish *that* purpose. This, even more plainly, appears in the case of the Joint Stock Banks. These institutions, *privately* financed, owned and controlled, never handle a penny of government money, even *temporarily*. They might, perhaps, be a proper part of a scheme of farm credits, but they are and can be no part of any machinery for expending public money. Their real purpose is to afford the opportunity for large investors to escape the payment of just taxes, a thing for which they are always looking.

These contentions go to the very root of the matter. No one can read the Act without being convinced, beyond a doubt, that the appropriation was a means to carry into effect the legislation and not the legislation a means to carry into effect the appropriation. Unless Congress can legalize, as it cannot (*Kansas* v. *Colorado*, 206 U. S. 46, 88, 89), *any* Act thought by it to be beneficial by appending an appropriation to carry it into effect, then the power here attacked cannot be *implied* from the right to appropriate money. If Congress can so act, then it can organize corporations to manufacture farming implements or to build workingmen's cottages or lawyers' homes or to reclaim arid lands or to furnish water to cities, provided only that there is some appropriation of public money. Doubtless such organizations would always succeed in spending the money, but that fact

alone would not justify them as a proper means for the execution of the powers of Congress.

As an intelligent writer (10 Lawyer and Banker and Southern Bench and Bar, October, 1917, p. 402) said:

> "Should the Supreme Court sustain this right, and hold that the 'Federal Farm Loan Act' is constitutional, *a fortiori,* every corporation having to do with the means of preserving the government would be exempt, and it is safe to assert that, once the inroad is made, all such corporations, with their subtle, powerful influence, would soon open the road and enlarge it to such an extent that they would all be traveling it; the states would necessarily cease to be, and then there would be a single government, and that in the hands of the corporations."

(c) An appropriation, even if made, cannot be used as a mere pretext to cover the exercise of an unauthorized power (*Supra,* Div. VI, subd. 5th, 6th). The present is a striking example of the attempt. Though the public money now invested was really advanced as a loan and will shortly be returned to the government, the pretended means for spending can go on forever, functioning a complete system for doing, in the various states, a *private* farm loan business. Dealing wholly in *private* capital, with not a cent of *public* money invested or to be invested, the banks, without any additional charter, will remain *forever* justified by the thought that they *once* assisted in spending some *public* money *conditionally* appropriated for *temporary* use in *establishing the very agencies in*

question. Congress has no power to create corporations for the purpose of handling an appropriation whose term of existence is not limited to the duration of the appropriation, but whose essential functions do not come into full play until after the repayment of the public money, and continue thereafter indefinitely as *private* corporations conducting *private* business. The designation of the agencies as depositaries of public money, *if and when desired,* is, as already shown (*Supra,* Div. V, subd. 4th), a minor provision, *incidental* to the *main* purpose, which cannot alone justify the entire scheme. It is a mere *incident* to a *private* business in a *private* interest. If it justifies the scheme, then Congress can create corporations to exercise powers of the widest latitude in *any kind* of business simply by designating them as depositaries or fiscal agents, though, as here, they were never intended to and never did act as such. These mere designations cannot make the corporations appropriate to the end in view, if otherwise they would be inappropriate (*Supra,* Div. V, subd. 5th).

(7th) *It would be a mere pretext to justify the Act as an appropriation authorizing the creation of corporations for unlimited periods to loan unlimited sums to farmers and forever exempt their assets and obligations from any kind of state taxation.*

(a) Even if the power to appropriate money could possibly be exercised through the creation of a corporation to handle the appropriation, still

that would not give the right to create one whose *principal* business was in the form of an activity other than dealing with the appropriation; nor could such corporation be used *chiefly* to enable *private* persons to loan their money or invest in its bonds. In no event could Congress authorize, as it attempted to, the creation of a corporation which, *after* spending the alleged appropriation, could go on, without more, fully authorized to continue indefinitely the *private* business of money lending. This would merit the condemnation (*M'Culloch* v. *Maryland,* 4 Wheat. 318, 423) of Mr. Chief Justice Marshall that:

> "Should Congress *under the pretext of executing its powers* pass laws for the *accomplishment of objects not intrusted to the Government,* it would become the painful duty of this tribunal * * * to say that such an act was not the law of the land."

(b) Besides agriculture, there are many other subjects of national concern, such as the problems of personal morality, education of children, insurance of lives against death, disability, accident and disease, and the protection of property.

If Congress, under the power of appropriation, *temporarily* exercised to a *limited* amount, can create a great system of *private* money lending, there is no limit to which the exercise of the power may be carried. For instance, the protection of property against fire and lives against death are matters affecting every one. By a small *temporary* appropriation to capital stock, Congress could acquire the power to create,

through private capital, gigantic life and fire insurance companies which would furnish money to persons suffering losses from fire or death in return for low premium rates. The immense capital thus invested, and payments made for death and for losses and those received from the members and the investment thereof could, on the same reasoning, be exempted from state taxation. The conservation and development of coal, timber, water power and the like are matters of great concern which directly affect the general welfare. Congress could, by small, temporary subscriptions to capital stock, authorize the creation of a "Conservation and Development Bank" to lend money at low rates to the owners, taking mortgages therefor and issuing its collateral bonds against them, all of which should be exempt from all state taxation. So, without appropriating any money, it could also authorize *private* capital to organize Joint Stock companies to engage in the same business, likewise exempting their bonds and mortgages from taxation.

Again, the irrigation of arid lands is a public purpose (*Fallbrook Irrigation Dist.* v. *Bradley*, 164 U. S. 112; *Houck* v. *Little River Dist.*, 239 U. S. 254). Congress could, in order to stimulate the irrigation of privately owned arid lands, authorize the creation of two classes of Irrigation Banks, one to which it would make a small temporary subscription for capital stock, and the other wholly organized by private individuals. It could authorize such banks to issue irrigation bonds secured by mortgages upon the irrigated lands. These could be exempted from state taxation. The

principle established by *Kansas* v. *Colorado*, 206 U. S. 46, 87-89, would thereby be destroyed.

Education, no less than agriculture, is a matter of national concern and welfare. Congress could, by a similar temporary appropriation for capital stock, authorize the creation of a corporation, free from state tax, for the purpose of furnishing money to promote the cause of universal education and authorize it to lend money at low rates. This money could be loaned only to persons building or operating school houses, colleges, technical or professional schools, and secured by mortgages on the plants and on the tuition fees of the students. It could exempt such bonds and mortgages from state taxation. It could authorize men like Mr. Rockefeller and his associates to create a joint stock company with hundreds of millions of capital to be loaned or otherwise expended in assisting persons engaged in educational work and withdraw from state taxation all such funds, together with the mortgages executed by the educators in return for the loans. So, Congress cannot regulate child labor (*Hammer* v. *Dagenhart*, 247 U. S. 251). Yet, it could, under the power of appropriation, create a corporation in which *private* capital could be invested for the purpose of discouraging child labor in factories. This by lending money at low rates of interest to those factories who would refuse to employ child labor. It could exempt from state taxation all the money earned, the loans thus made and the mortgages thus taken, as well as the bonds issued against them. The congressional appropriation soon being returned to

Congress (as the farm loan appropriation is being returned), there would exist, without further charters, huge mortgage lending and money earning companies assisting factories, all of whose operations and investments would be exempt from state taxation. Congress, by the same expedient of a trifling appropriation, could permit men like Mr. Rockefeller and his associates to organize a corporation having for its object the suppression of vice, by means of loans at low rates, or bounties paid, to immoral people in order to assist them in abandoning their vicious careers and getting a new start in life. The capital thus invested, the loans taken from the unfortunate people and the bonds issued thereon could be exempted from state taxation.

The development of the agricultural interests does not more greatly affect the general welfare nor is it a more important public purpose than the alleviation of poverty and unemployment. By the same system of appropriation, Congress could authorize philanthropists to organize corporations, likewise exempt from taxation, by which immense sums of private capital may be devoted to loans to the poor or unemployed, either without security or secured by chattel mortgages, assignments of salaries, or future earnings or otherwise. These examples could be multiplied indefinitely. Suffice it, Congress, on the same reasoning, could aid any situation, by authorizing *private* individuals to embark in any *private* business, regardless of its substantial relation to the execution of a federal power.

(c) The power to borrow money on the credit of the United States does not authorize the issuance and sale of Farm Loan Bonds to private investors, nor the exemption thereof from state taxation.

While Congress has the power "to borrow money on the credit of the United States," the Farm Loan Bonds do not represent the exercise of any power by Congress to borrow money on the credit of the United States. Congress does not borrow the money. The money is not borrowed on the credit of the United States. No money realized from the sale of the bonds is placed in the United States Treasury. None of the proceeds belong in any way to the United States. The disposition thereof is not made by Congress, but by the directors of the Land Banks who are not public officials. Farm Loan Bonds are neither an asset nor a liability of the government. Congress voted down an amendment to guarantee the bonds, which shows that it did not intend to be considered responsible therefor (*United States* v. *Del. & Hudson R. R. Co.*, 213 U. S. 366, 414). The government disclaims any liability on the bonds (Farm Loan Primer, Ans. 102). Mr. Carter Glass said in a debate that the government "took a very limited *temporary* stake in the system"; that he did *not* consider the Farm Loan system a government "instrumentality," and that he disagreed with the opinion of Ex-Justice Hughes that the United States was *morally* bound on the bonds.

Money obtained from *private* investors by the sale to them of bonds issued by the Land Banks

and secured by the farm mortgages of private farmers, is not money borrowed on the credit of the United States, and is not an exercise of the congressional power to borrow money.

(8th) *The power to appropriate money does not authorize Congress to do more than distribute the money appropriated. It does not authorize the creation of private corporations to do a private business.*

Article I, section 8, clause 1, of the Constitution provides:

> "The Congress shall have power to lay and collect taxes, duties, imposts and excises, *to pay the debts and provide for the common defense and general welfare of the United States.*"

Although the subject of much discussion, it was decided in *Kansas* v. *Colorado*, 206 U. S. 46, and may be considered as settled, that the italicized words did not confer on Congress any substantive power to provide for the country's general welfare, nor are they merely harmless introductory words limiting the subsequently enumerated powers.

(Federalist No. 41; Jefferson's "Opinion on the constitutionality of a National Bank," February 15, 1791; Jefferson's letter to Gallatin, June 16, 1817; Madison's veto of the Bonus Bill, March 3, 1817; Monroe's veto of the Cumberland Road Bill, and his Views of the President of the United States on the Subject of Internal Improvements, May 4, 1822; Madison's letter to Steven-

son, November 17, 1830; 3 Farrand's Records of Federal Convention, 483; Story on Constitution, sections 907-930; 1 Willoughby on Constitution, sec. 22; 1 Tucker on Constitution, secs. 222-223; 1 Hare's Am. Const. Law, 241-242; 1 Watson on Constitution, 398; 10 Fed. Stat. Ann. 403 and authorities cited; *Van Brocklin* v. *Tennessee*, 117 U. S. 151, 158.)

The accepted view is that Congress has power to lay and collect taxes *for the purpose* of paying the debts and providing for the common defense and general welfare, thereby *qualifying the objects* for which taxes may be laid.

Despite the powerful arguments of many statesmen, the views of Mr. Hamilton, in his Report on Manufactures, have prevailed in actual practice, namely, that Congress can appropriate money raised by taxation for any purpose or object which it deems conducive to the *general*, as distinguished from *local*, welfare; and such action is almost, if not entirely, beyond the control of judicial power. While practically there are few, if any, limitations on the power of Congress to *appropriate* money, all the authorities are agreed that *the power is exhausted upon the application of the money*. Mr. Hamilton, in his Report on Manufactures (December 5, 1791), said:

> "It is, therefore, of necessity, left to the discretion of the national legislature to pronounce upon the objects which concern the general welfare, and for which, under that description, an appropriation of money is requisite and proper. And there seems to be no room for a doubt that whatever concerns

> the general interests of learning, of agriculture, of manufactures, and of commerce, are within the sphere of the national councils, *as far as regards an application of money.* • • • No objection ought to arise to this construction, from a supposition that it would imply a power to do whatever else should appear to Congress conducive to the general welfare. *A power to appropriate money* with this latitude, which is granted, too, in express terms, *would not carry a power to do any other thing* not authorized in the Constitution, either expressly or by fair implication."

President Monroe, in his "Views of the President of the United States on the Subject of Internal Improvements," accompanying his veto of the Cumberland Road Bill (which is universally conceded to be the most thorough and elaborate view which has ever been taken of the subject of Congress's power to appropriate money) was of the opinion that Congress could appropriate money to any purpose which it deemed conducive to the general welfare, *but that it could go no further than to appropriate the money* and could not undertake the projects to which the money was applied.

After disposing adversely of Mr. Madison's contention that the power of appropriation was limited to the execution of the powers enumerated or implied therefrom, Mr. Monroe (II Messages and Papers of the President, p. 167) said:

> "If, then, the right to raise and appropriate the public money is not restricted to the expenditures under the other specific grants

according to a strict construction of their powers, respectively, is there *no limitation* to it? Have Congress a right to raise and appropriate the money to any and to every purpose according to their will and pleasure? They certainly have not."

He then argues that the money can be appropriated to any great national purpose, including good roads, canals, foreign concerns, and (p. 168) says:

"The right of appropriation is nothing more than a right to apply the public money to this or that purpose. *It has no incidental power, nor does it draw after it any consequences of that kind.* All that Congress could do under it in the case of internal improvements would be to appropriate the money necessary to make them. For every act requiring legislative sanction or support, the State authority must be relied on. The condemnation of the land, if the proprietors should refuse to sell it, the establishment of turnpikes and tolls, and the protection of the work when finished must be done by the State. To these purposes the powers of the General Government are believed to be utterly incompetent."

In his accompanying veto message Mr. Monroe said:

"A power *to establish* turnpikes with gates and tolls, and to enforce the collection of tolls by penalties, *implies a power* to adopt and execute a complete system of internal improvement. A right to impose duties to be paid by all persons passing a certain road, and on horses and carriages, as is done by this bill, involves the right to take the land from the

> proprietor on a valuation and to pass laws for the protection of the road from injuries, and if it exist as to one road it exists as to any other, and to as many roads as Congress may think proper to establish. A right to legislate for one of these purposes is a right to legislate for the others. It is a complete right of jurisdiction and sovereignty for all the purposes of internal improvement, *and not merely the right of applying money under the power vested in Congress to make appropriations*, under which power, with the consent of the states through which this road passes, the work was originally commenced, and has been so far executed. I am of opinion that Congress do not possess this power; that the states individually cannot grant it, *for although they may assent to the appropriation of money* within their limits for such purposes, they can grant no power of jurisdiction or sovereignty by special compacts with the United States. This power can be granted only by an amendment to the Constitution and in the mode prescribed by it."

Andrew Jackson, in vetoing the Maysville Road Bill, with reference to the appropriation of money (*id.*, p. 488), said:

> *"No aid can be derived from the intervention of corporations.* The question regards the *character* of the work, not that of those by whom it is to be accomplished."

Mr. Madison, in vetoing the Bonus Bill on March 3, 1817 (*id.*, Vol. I, p. 584), said:

> "A restriction of the power 'to provide for the common defense and general welfare' to

> cases which are to be provided for *by the expenditure of money* would still leave within the legislative power of Congress all the great and most important measures of government, *money* being the ordinary and necessary means of carrying them into execution."

In 1 Willoughby on the Constitution, it is (sec. 269) said:

> "In fact, however, the limitation that an appropriation should be for a public purpose has been without practical effect, as the courts have in no case attempted to hold invalid an appropriation by Congress on the ground that it has been for a purpose not public in character; and, as regards the restriction that appropriations shall be in aid of enterprises which the federal government is empowered to undertake, the doctrine has become an established one that Congress may *appropriate* money in aid of matters which the federal government is *not* constitutionally able to administer and regulate."

In 1 Hare's American Constitutional Law, pages 241-250, there is an admirable review of the whole subject, including many of the historic instances involving the appropriation of money by Congress. He points out that the construction of railways, high roads, bridges and other internal improvements is derivable, *not* from the power to *appropriate money*, but from the war, postal and commerce powers. Referring to certain appropriations it is said:

"In the greater number of the instances above referred to, the government did not act in its sovereign capacity, *but like a rich and public-spirited individual who draws his pursestrings for the common good;* and therefore they do *not* tend to show that Congress may, by virtue of the eighth section of the first article, devise internal improvements and enact such laws as are necessary and proper to render the scheme effectual.

It is one thing to construct a highway by virtue of the power of eminent domain, and exercise an absolute jurisdiction over it when made, *and another to lay out a road through land acquired by purchase* with the consent of the state through which it passes. So Congress may well be entitled to *appropriate money* for public education, or even to build and endow colleges and schools, *and yet want the right to make attendance compulsory and enforce it by fines or penalties.*"

It is also there said:

"In other words, although the United States may go into the market and do whatever can be done by the use of money without the exercise of legislative, executive, or judicial power, they cannot, speaking generally and where there are no special grounds, do more."

In Tucker on the Constitution, Vol. 2, secs. 222-234, there is elaborate consideration of the entire subject; and it is pointed out that if Congress, under the power of appropriation, can supervise and intervene in the administration of the project to which the money is applied, our government

would be exercising a power not conferred upon it.

The extent of the power of appropriation has never been determined by the court. (*Field* v. *Clark*, 143 U. S. 649, 695; *U. S.* v. *Realty Co.*, 163 U. S., 427, 433.) But for the purposes of this argument, the right of Congress to appropriate public money to any purpose it may desire need not be questioned. It is, however, insisted that the power to appropriate for the general welfare is limited to the disbursement of money, with, at most, such machinery for its application to the desired end as may be used without the exercise of federal power to abridge the rights of the states or the citizens thereof. This is a very different thing from the creation of *private* corporations whose *chief* and *only* purpose is to loan cheap money to farmers.

VII.

The exemption from taxation is unwarranted.

(a) Under Section 21, each Land Bank bond *must* recite "that it is not taxable by *national, state* or *municipal* authority." Section 26 specifically exempts Land Banks and Farm Associations from practically *all* taxation. It also likewise exempts *all* Land Bank and Joint Stock Bank *farm* loan mortgages and bonds, and the income therefrom, declaring them to be "instrumentalities of the government." The validity of these provisions is separately challenged. The enormous value of this exemption has been (Statement, Div. 6) already adverted to.

(b) If, of course, the Act is unconstitutional as to either class of banks, no tax exemption can, as to that bank, be upheld, because as Mr. Justice Field in *Norton* v. *Shelby County*, 118 U. S. 425, said:

> "* * * an unconstitutional Act is not a law, it confers no rights, it imposes no duties, it affords no protection, it creates no office; it is in legal contemplation as inoperative as though it has never been passed."

This by one of the counsel (Brief and Argument for Appellee Federal Land Bank of Wichita, Kansas, p. 17) is thus practically conceded:

> "The validity of that feature of the Act is a corollary to the determination of the validity of the provisions of the Act for the creation of the Federal Land Banks and for the issue of the Farm Loan Bonds. Congress expressly declared that these bonds should be deemed to be instrumentalities of the Government of the United States and as such should be certified by the federal officers composing the Federal Farm Loan Board as regularly issued and exempt from taxation. This question is thus not as to intent but as to power. And there is no room for controversy as to the power to give the prescribed immunity if Congress had the power to create these corporations and to provide for the issue of these bonds."

(c) While *real* governmental instrumentalities are exempt and should be exempted from *state* taxation (Willoughby on Constitution, sec. 45, *et seq.*), the exemption should never be lightly ex-

tended (*Thomson* v. *Union Pacific R. Co.*, 9 Wall. 579). This because Congress cannot (*Supra*, Div. V, subd. 5, 6) call something such an instrumentality and by such a simple method relieve it from state taxation. Otherwise, little by little, encroachments could be made until there is nothing left for a state to tax, and the state itself would fall for lack of revenue to support it. There must, therefore, be an *actual* and *essential* governmental instrumentality before, without more, it is or can by Congress be made exempt from any state tax. So, whatever Congress may do as to exempting property from a tax levied under its own authority, it cannot grant an exemption from a state tax unless the latter be levied upon that which is *really* an *essential* instrumentality of the government.

The power to tax exists concurrently in both the state and federal governments and is equally indispensable to the existence of each (*M'Culloch* v. *Maryland*, 4 Wheat. 316, 425; *Lane Co.* v. *Oregon*, 7 Wall. 71, 76, 77). There are certain *implied* limitations on the taxing power of both arising out of the very nature of our dual system. (*M'Culloch* v. *Maryland*, 4 Wheat. 316, 425, 426; *The Collector* v. *Day*, 11 Wall. 113, 123; *U. S.* v. *Railroad Co.*, 17 Wall. 322, 327; *Railroad Co.* v. *Peniston*, 18 Wall. 5, 30; *Dobbins* v. *Commissioners*, 16 Pet. 435, 447; *Van Brocklin* v. *Tennessee*, 117 U. S. 151, 157.) Any restriction upon the state's power to tax arises from the operation of the Constitution itself. Congress cannot, by any declaration of exemption, create one that would not have equally existed

without it (*id.*). In other words, any attempt by Congress to *exempt* property from state taxation, if valid, is merely declaratory of what the exemption would have been anyway, without such declaration (*id.*). So it was decided in *M'Culloch* v. *Maryland,* 4 Wheat. 316, 425, 426, and *Osborn* v. *Bank,* 9 Wheat. 738, 777, 794, 795, and such is the effect of the various cases, saying, as between the states and United States, what can and what cannot be taxed. Thus it has been held that the states cannot tax government bonds or other direct obligations of the United States (*Weston* v. *City of Charleston,* 2 Pet. 449; *Bank* v. *Supervisors,* 7 Wall. 26); nor bonds issued by municipalities in the territories established by Congress for the government of the people before their admission as states (*Farmers' Bank* v. *Minn.,* 232 U. S. 516) or by the District of Columbia (*Grether* v. *Wright,* 75 Fed. Rep. 742, 753, *et seq.*); nor land owned by the United States, either when purchased in pursuance of a governmental function, or acquired as a part of its territorial domain by a treaty or otherwise (*Van Brocklin* v. *Tennessee,* 117 U. S. 151); nor the receipts from coal mines owned by the Indians but operated by private parties under a lease from the government in pursuance of the government's treaty obligations to apply the revenues from the mines to the education of Indian children (*Choctaw & Gulf* v. *Harrison,* 235 U. S. 292); nor the salary of a federal official (*Dobbins* v. *Commissioners,* 16 Pet. 435); nor the necessary operation of a means adopted by the United States to execute its express powers (*M'Culloch* v. *Mary-*

land, 4 Wheat. 316; *Williams* v. *Talladega,* 226 U. S. 404, 418, 419); nor the franchise of a corporation created by Congress (*California* v. *Pacific R. R. Co.,* 127 U. S. 1); nor the tangible or intangible property (except real estate) of corporations organized primarily as instrumentalities of the government (*Owensboro National Bank* v. *Owensboro,* 173 U. S. 664).

It has also been held that Congress cannot tax the bond or obligations of a state or its municipal subdivisions (*Pollock* v. *Farmers Loan & Trust Co.,* 157 U. S. 429, 584; *Mercantile Bank* v. *New York,* 121 U. S. 138, 162); or the salary of a state official (*Collector* v. *Day,* 11 Wall. 113, 124); or municipal revenues (*U. S.* v. *Railroad Co.,* 17 Wall. 322).

The states can tax the property and operations of persons and corporations engaged in *private* business, although also employed by the federal government in the transaction of its *governmental* business. Accordingly, it has been held that a state can tax checks drawn by the United States in payment of its interest obligations, notwithstanding an attempted congressional exemption of United States obligations from state taxation (*Hibernia Savings Society* v. *San Francisco,* 200 U. S. 310), the personalty, credits, moneys, etc., of a railroad company chartered by Congress, financially assisted by it, and engaged in performing federal services (*Thomson* v. *Railroad,* 9 Wall. 579; *Railroad Co.* v. *Peniston,* 18 Wall. 5, 30-35; *Union Pacific* v. *Lincoln County,* 1 Dill. 314); while it is a matter of common knowledge that the states can tax and do tax many species of prop-

erty which are being used by agents of the United States as the means of executing powers of the government, such as telegraph lines, dredges and manufacturing plants (*Gromer* v. *Standard Dredging Co.*, 224 U. S. 362; *Baltimore Shipbuilding Co.* v. *Baltimore*, 195 U. S. 375, 382).

The principle underlying the cases is that neither the state nor federal government can tax the property or operations of any *essential* governmental instrumentality of the other.

The reason why the states can tax the property and business of railroads, telegraph lines, etc., although they may have been chartered by Congress and used in part as governmental instrumentalities, and yet cannot similarly tax national banks, lies in the distinction between the two instrumentalities. The railroad and telegraph lines could, in fact, perform all the services for the federal government just as well *without* the addition of private business as they can with it (except as a money making proposition); and hence in accordance with the express language of *Osborn* v. *Bank*, 9 Wheat. 738, 861, the property and private operations of the companies are generally taxable by the state. The banks, as pointed out in that case and in *M'Culloch* v. *Maryland*, 4 Wheat. 316, could only satisfactorily perform their essential *governmental* duties by being endowed with the right to transact private business; as private banking business was the very thing which was needed to enable them to be an efficient machine for carrying out their fiscal operations.

A Joint Stock Bank, acting as a depositary, could, like the railroads, perform such a function

just as satisfactorily to the government without, as with, the addition of private business. This is an additional reason why the Joint Stock Banks fall as depositaries into the category of the railroads and not of that of the national banks.

The mere *possibility* that at some future time the United States may elect to *designate* a Land or Joint Stock Bank as a depositary and thereafter may further elect actually to use it as such, while in the meantime the corporation is engaged solely in *private* business for *private* gain, certainly does not constitute the corporation such an *essential* instrumentality of the federal government as to exempt it from state taxation. So it was decided in *Baltimore Shipbuilding Co.* v. *Baltimore*, 195 U. S. 375, 382. There an old government fort (of course not taxable) was conveyed to a shipbuilding company upon condition that it would construct a dry dock thereon; that the United States should have the right to use it forever free of charge, and that if its use as a dry dock was ever abandoned the property should revert to the United States. It was held that the property was subject to *state* taxation. Mr. Justice Holmes said:

> "It would be a very harsh doctrine that would deny the right of the states to tax lands because of a *mere possibility* that they might lapse to the United States."

Whether such loans or bonds are or can be made *governmental* instrumentalities, depends upon whether the *main* purpose of the agency issuing them is to exercise a *governmental* function, or

one that pertains to *private* or *proprietary* interests (*Supra*, Div. V). Hence, in the end, this may be concluded: If the *main* and *essential* purpose of either agency is to exercise a governmental function, to which the exercise of *private* powers is a mere incident, an exemption from *state* taxes exists as to that particular agency. It is otherwise if the *main* and *essential* purpose is to exercise a *private* function, to which the *governmental* powers are mere *incidents*.

VIII.

Even if the Act and its tax exemption feature can be upheld as to the Land Banks, they cannot be sustained as to the Joint Stock Banks.

(a) As an evident after-thought and to enable *large* investors to escape *all* kinds of income taxation, *some* person by *some* inconceivable method, convinced Congress that it should, as it did (sec. 16) provide for *other* unrestricted *money-making* agencies, in *addition* to the Land Banks, owned and controlled by *outsiders*, to deal only with the *large* investors. These other and unrestricted *outside* agencies are federal corporations known as Joint Stock Banks.

(b) They, *without limit in numbers*, can, with nothing but the approval of the Board, be organized by *any* ten or more *natural* persons, regardless of their being borrowers. Neither the government, Farm Association nor Land Bank has any connection therewith nor any interest therein, nor can either hold any of their stock. The organiza-

tion is thereby in each instance, without restrictions, made up of *outsiders* and kept in the hands of those who happen to be *favored* by the Board. The sole corporate purposes are to loan, in *unlimited* amounts, on *farm* mortgage security and issue collateral trust farm loan bonds secured thereby. Such an institution must have, at least, five directors. All stock has a double liability, and the stockholder has the same voting privilege as a stockholder in a national bank. It can (sec. 16) receive no money on deposit. It can do no *general* banking or other business. It has (Bill, Rec. 10) never done any. Its *sole* business is to loan on *farm* mortgages, and issue and sell bonds secured thereby. $250,000 of its capital must be subscribed and one-half thereof paid up. To issue any bonds, all the capital must be paid. It has, except when otherwise specifically provided, the same powers and is subject to the restrictions and conditions imposed on Land Banks, but only so far as the same may be applicable. Practically every feature which led to or could justify the organization of Land Banks is declared to be inapplicable. Thus, interest rates of Joint Stock Banks cannot, as in the case of Land Banks (sec. 17, subd. [b]) be reduced by the Board so as to make any equalization thereof; their loans, as required in the case of those of Land Banks (sec. 12, subds. 1, 4, 6, 7, 10), need not be secured on *farm* lands in the banking district, nor made to *cultivators* of land, nor the proceeds thereof used to buy or improve the farms, nor the amount of each loan limited to $10,000, nor the borrowers required to agree that if the whole or any portion of the loan

be expended for purposes other than those specified, or if there be any other default, the whole amount shall become due. The borrowers cannot, as in the case of the Land Banks, use part of the loan to pay for any stock in a Farm Association. The only substantial limitation is that the loans shall be made if secured by *first* mortgage on *farm* lands within the state in which the Joint Stock Bank is located or one contiguous. Presumably, as a source of *private* profit to this outside agency, the interest charged on a mortgage loan can exceed by one per cent the rate established by the last series of farm loan bonds issued. All bonds, while in a form prescribed by the Board, must have added thereto the words "Joint Stock," and by engraving, form and color be made distinguishable from Land Bank bonds.

(c) A Joint Stock Bank, like a Land Bank, *can be designated* as a depositary of public moneys, or *may* be (sec. 6) employed as a financial agent of the government. It is not required to be. Even this, however, is not the *main* purpose of the Act, but rather a mere *incident* to the *private* business done for the *private* interest. Or else it is a mere device or subterfuge in an attempt to make constitutional a statute which otherwise would be unconstitutional. However, it has never acted as a bank, received current deposits or in any wise acted as a government depositary or financial agent (Bill, Rec. 10).

(d) As if Congress had not done enough for the outsiders' profit-making machine and the large investors' tax exemption haven, all Joint Stock farm loan bonds are made lawful investments for

fiduciary and trust funds, they are permitted to be used as security for public deposits and may be bought and sold by any bank of the Federal Reserve System.

(e) All farm mortgages taken and all farm loan bonds issued are (sec. 26) declared to be "instrumentalities of the government," and all income therefrom actually exempted from *all* federal, *state* and municipal taxes.

(f) Large investors have not failed to profit by the organization of these banks. Twenty-seven of them have been organized (Bill, Rec. 9), and up to October 31, 1919, they had paid in $7,812,050 of capital, issued $46,255,000 of farm loan bonds, of which $41,000,000 are still outstanding (Bill, Rec. 11; Report 317, Senate Bill No. 3109, Calendar No. 270, 66th Congress, 2d Session). So un-American are these institutions, and so unfair to the public is the withdrawal by *large* investors of *large* investments from taxation that the Senate Committee on Currency and Banking has favorably reported (Report 317, Appendix, Part 2, the original Appellant's Brief, p. 91) a bill (Appendix, art 3; *id.*, p. 94) to repeal, *for the future*, all tax exemptions of the loan bonds because "the tax exemption privilege ought never to have been extended," and "the accumulation of large aggregations of capital, wholly exempt from any and all forms of taxation, is wrong in principle and should be discontinued." The committee was of the clear opinion that "the *large* taxpayers will gradually absorb these bonds, which will contribute *nothing* to the support of the government."

In a very recent strong article in his own magazine (41 Farm and Home, No. 849, p. 6, January, 1920) headed "A National Scandal," Herbert Myrick, the reputed "Father of the Federal Loan Act," concluded:

> "The weak spot can be found, even in the best of things. The federal farm loan system is no exception. The nigger in the wood pile stands revealed. *It is in the section which authorizes Joint Stock Land Banks.* • • • 'Why, the thing is a national scandal,' truly remarked Senator Knute Nelson of Minnesota in a recent conversation. The Senator spoke wisely."

This same father of the Federal Farm Loan Act has written (41 Farm and Home, No. 854, June, 1920, p. 8) this:

> "The law's delays are again observable in the federal farm loan system. Its case in the United States Supreme Court is to be reargued, and decision may not be reached until the year's end. Meanwhile the whole system is shut down, because until the court decrees that federal farm loan bonds are tax exempt they cannot be sold for funds to lend to farmers on mortgage.
>
> My opinion is that the weak link in the law is its authorization of joint stock land banks for private profit. It was a mistake to insert that section in the law. Outright repeal by Congress of that section is the only safe thing to do now. The bill favorably reported to House for liquidating the joint stocks is not enough.

The true co-operative federal land banks, purely mutual, not for profit, owned by and operated for borrowing farmers, should not be jeopardized by the section objected to.

Purchase by the treasury of $100,000,000 of farm loan bonds issued by federal land banks (not joint stock), proposed in a pending bill, will help to tide over the present situation, but is only a makeshift. Farmers don't ask for pap, they only want their co-operative farm loan system to have a free field and no favors. Meanwhile the old-style mortgage brokers are again waxing fat, following their temporarily successful attack through the courts upon the bank system. Curious how many folks want to deprive the farmer of any good things."

Congress has, in fact, already, to a certain extent, at least, recognized that the Joint Stock Banks have no real reason for longer existence. By the Act of May 29, 1920, it is provided that they *may* be speedily liquidated. That Act (264 Fed. Rep. 503, 504) reads:

"JOINT STOCK LAND BANKS.

§9835hh. (Act July 17, 1916, c. 245, §16, as amended, Act May 29, 1920, c. ———.)

(12) Voluntary liquidation.

Any joint-stock land bank organized and doing business under the provisions of this Act *may* go into voluntary liquidation by making provision, to be approved by the Federal Farm Loan Board for the payment of its liabilities: Provided, That such method of liquidation shall have been duly authorized by a vote of at least two-thirds of the shareholders of such joint-stock land bank at a

regular meeting, or at a special meeting called for that purpose, of which at least ten days' notice in writing shall have been given to stockholder.

(13) Same; powers of Federal land bank.

For the purpose of assisting in any such liquidation duly authorized as in the preceding paragraph provided, any Federal land bank *may,* with the approval of the Federal Farm Loan Board, acquire the assets and assume the liabilities of any joint-stock land bank, and in such transaction may waive the provisions of this Act requiring such land bank to acquire its loans only through national farm loan associations, or agents, and those relating to status of borrower, purposes of loan, and also the limitation as to the amount of individual loans.

(14) Same; preceding paragraph limited.

No Federal land bank shall assume the obligations of any joint-stock land bank, in such manner as to make its outstanding obligations more than twenty times its capital stock, except by the creation of a special reserve equal to one-twentieth of the amount of such additional obligations assumed."

One, the Wichita, Kansas, Joint Stock Bank, is now understood to be in the process of liquidation under this Act.

(g) Abandoning all the reasons for the use of the Land Banks, Congress, as an apparent afterthought, conceived the notion of having established Joint Stock Banks. Had these, in the first instance, been provided for, Land Banks would have been unnecessary, and nine-tenths of the

entire Act could have been dispensed with. The government has not the slightest connection with the Joint Stock Banks, and can never have any interest therein. Individuals, not necessarily borrowers, *only* can organize, own and control same. These *alleged* banks can loan to *any one* on farm lands, in *unlimited* amounts and without *any* restrictions as to the use made of the land or to be made of the money borrowed thereon. The extent of their calling is to loan on *farm* mortgages and issue and sell their own bonds with the mortgages as security.

Not only is there a difference between the Land and the Joint Stock Banks as to the ownership and control thereof, but, in the case of the Land Banks, the loans are made to *farm* occupants in *restricted* amounts and for *specific* purposes, while with the Joint Stock Banks there are no restrictions as to amount, persons or purposes. While in this way non-cultivating farmers, or even speculators, can borrow on vacant land and on easy terms, the large investor really reaps the greatest benefit, for he, by a private investment of private funds, is permitted to go tax-free. In the practical working out of the scheme, still more pointed and detailed distinctions have been observed. The *alleged* advantages to *large* investors of *tax-free* Joint Stock Bank bonds have, *pending the litigation,* been made the subject of such advertisements as should shame even eager and keen-minded selling brokers. All this has been a subject of congressional attention, the details of

which appear in a government printed document of November 13, 1919, entitled:

> "Amendment to Federal Farm Loan Act. Hearings before the Committee of Banking and Currency of the House of Representatives on H. R. 8159, a bill to amend the Act of Congress, approved July 17, 1916, known as the Federal Farm Loan Act, to increase the limit of loans."

(h) So, even if any reason can be found to sustain the Act or the tax exemption therein as to the Land Banks, there is no fair reason for so doing as to Joint Stock Banks.

The lower court (Rec. 27-29) really so recognized by saying:

> "Now as to the Joint Stock Land Banks and their Farm Loan bonds, of course, I think all those present will admit that there is a possible line of cleavage between the two. That is to say, it would appear, almost, that you could take some sharp instrument and cut the Joint Stock Land Banks out of the Act, and that the Federal Land Banks and their bonds would function just the same. That is, there is no absolute connection, in so far as the system, as a system, is concerned, between the two, but it has been pointed out that these banks are to serve a different class of customers, those who require larger loans; that they have a distinct function to perform, along the same line as the Federal Land Banks.
>
> They are incorporated into the same Act. We cannot leave out of mind that one great system is here being created, comprehensive

in its nature, containing many parts, and all so interwoven and interrelated that each performs its appointed part in the development and administration of the entire system.

It may be said—perhaps the Supreme Court may say—that they are so far separated from, and not so necessarily connected with the system that they may be taken out, taken apart, and dealt with separately, but certain it is that they are thoroughly germane to the system, and certain it is that they have been dealt with in one comprehensive, systematic plan.

That being so, it does not seem to me, when I take into consideration the fact, also, that they have been, even though arbitrarily, created depositaries of the government, created as financial agents of the government, that the arguments against them are so clear and convincing as they must be to warrant a court of first instance to overcome the presumption of constitutionality which must prevail, and to declare these Acts unconstitutional, even as to the Joint Stock Land Banks.

I am aware that in a certain very conspicuous instance, the court, in the interest of expedition, has deemed it wise to indulge the presumption of unconstitutionality in the first instance, instead of constitutionality. That is something that I cannot bring my mind to accept, and when these banks are thus designated as banks—as depositaries, and as financial agents, why, if the use is conceded in any degree, this court cannot consider the degree of their usefulness in that regard.

It stands there as the deliberate judgment of Congress that they are such, they are adapted to the use—even though their powers may have to be enlarged to make them most

useful, they are adapted to the use that Congress has assigned them. That being so, all things considered, and there being no question here, nor can be in this court, as to the wisdom and practicability of this system, then in the absence of any complete unadaptability, the court must accept their status as declared.

But whatever might be my view on these Joint Stock Banks, certainly the matter must go to the Supreme Court.

Upon one branch of the question, as I say, I am unreservedly without doubt. Upon the other, I may say, also, that I have very little, if any, doubt, although I concede that there is a more debatable question there presented, but certainly there ought not to be a division of the questions here involved.

There ought not to be any action taken which would halt a great public enterprise, certainly, as has been pointed out, to the very great disadvantage of its operation, and of the interests of parties who are dealing with it, but the whole question should be passed upon finally, as speedily as possible, and with the least inconvenience to anyone concerned, by the Supreme Court * * *."

But, after so saying, the Act was below upheld as to the Joint Stock, as well as the Land Banks. That this was possible seems inconceivable.

Respectfully submitted,

WM. MARSHALL BULLITT,
FRANK HAGERMAN,
Solicitors for Appellant.